

The California Commission on Health and Safety and Workers' Compensation



Selected Indicators in Workers' Compensation: A Report Card for Californians

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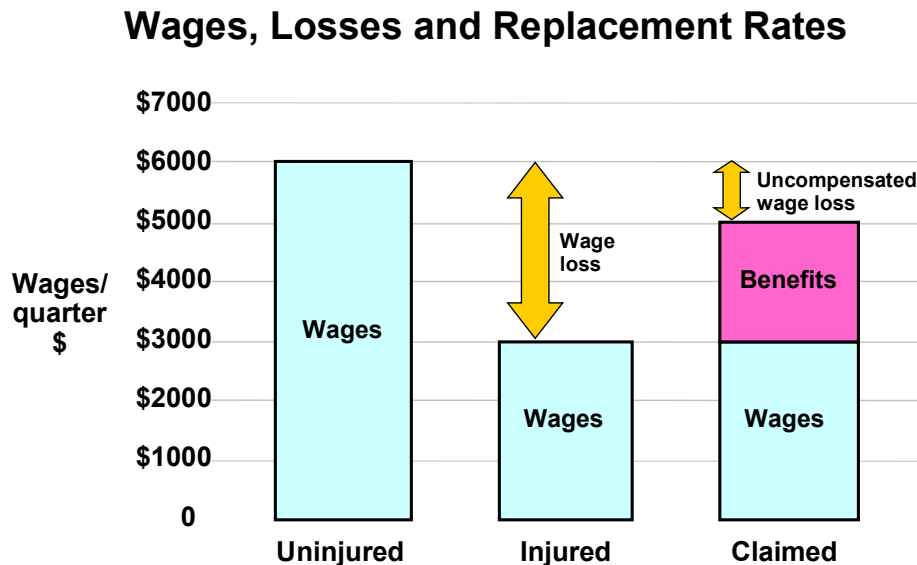
Workers' Compensation System

Pre-2004 Reform Benefits

Wages, Losses and Replacement Rates

CHSWC studies by RAND analyzed wage losses sustained by permanently disabled workers and the replacement rates or the extent to which workers' compensation benefits compensated for the wage loss.

The studies have shown that some workers experience significant wage losses after a workplace injury.

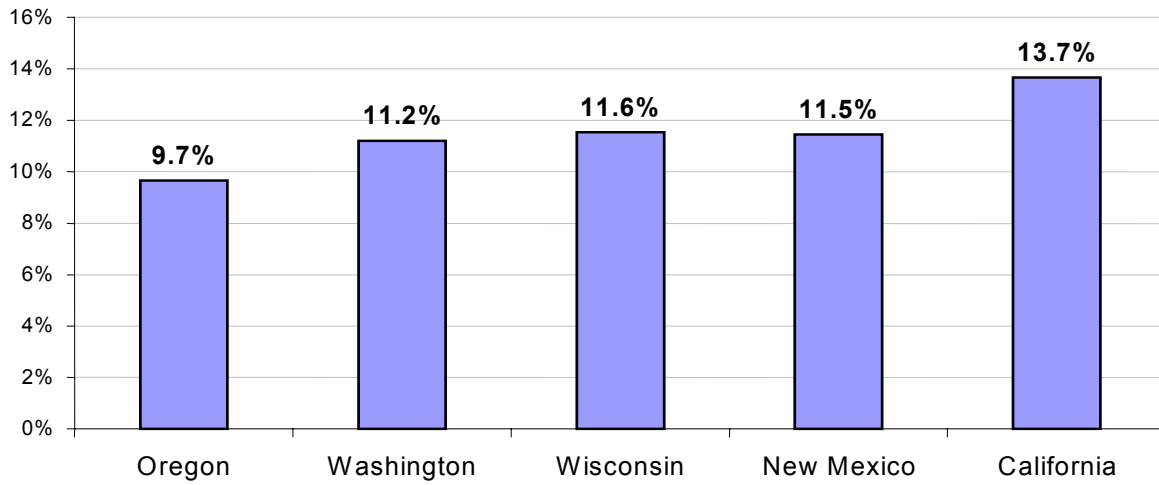


Wage Loss = \$3000 Proportional Wage Loss = 1/2 Replacement Rate = 2/3

Source: CHSWC Study of Permanent Disability by RAND

Pre-Reform Return-To-Work Indicators

Percentage of PPD Claimants Out of Work After 3 Years



Source: RAND

Workers' Compensation Premiums

Pure WC Premium Advisory Rates

Open Rating

In 1993, the workers' compensation reform legislation repealed California's 80-year-old minimum rate law and replaced it beginning in 1995 with an open-competition system of rate regulation in which insurers set their own rates based on "pure premium advisory rates" developed by the WCIRB. These rates, approved by the IC and subject to annual adjustment, are based on historical loss data for more than 500 job categories.

Under this "open rating" system, these recommended, non-mandatory pure premium rates are intended to cover the average costs of benefits and loss-adjustment expenses for all employers in an occupational class and thus provide insurers with benchmarks for pricing their policies. Insurers typically file rates that are intended to cover other costs and expenses, including unallocated loss-adjustment expenses.

The chart on the following pages shows the history of the workers' compensation pure premium advisory rates since the 1993 reforms.

**Advisory Workers' Compensation Rates:
A History Since the 1993 Reform Legislation
Part One: 1993 – 2000**

1993

Insurance Commissioner approved:

Pure premium rate reduction of 7 percent effective July 16, 1993, due to a statutory mandate.

1994

WCIRB recommendation:

No change in pure premium rates.

Insurance Commissioner approved:

Two pure premium rate decreases: a decrease of 12.7 percent effective January 1, 1994; and a second decrease of 16 percent effective October 1, 1994.

1995

WCIRB recommendation:

A 7.4 percent decrease from the pure premium rates that were in effect on January 1, 1994.

Insurance Commissioner approved:

A total of 18 percent decrease to the premium rates in effect on January 1, 1994, approved effective January 1, 1995 (including the already-approved 16 percent decrease effective October 1, 1994).

1996

WCIRB recommendation:

An 18.7 percent increase in pure premium rates.

Insurance Commissioner approved:

An 11.3 percent increase effective January 1, 1996.

1997

WCIRB recommendation:

A 2.6 percent decrease in pure premium rates.

Insurance Commissioner approved:

A 6.2 percent decrease effective January 1, 1997.

1998

WCIRB recommendation:

The initial recommendation for a 1.4 percent decrease was later amended to a 0.5 percent increase.

Insurance Commissioner approved:

A 2.5 percent decrease effective January 1, 1998.

1999

WCIRB recommendation:

The WCIRB initial recommendation of a 3.6 percent pure premium rate increase for 1999 was later amended to a recommendation for a 5.8 percent increase.

2000

WCIRB recommendation:

An 18.4 percent increase in the pure premium rate for 2000.

Insurance Commissioner approved:

An 18.4 percent increase effective January 1, 2000.

**Advisory Workers' Compensation Pure Premium Rates
A History since the 1993 Reform Legislation
Part Two: 2001 - 2003**

2001

WCIRB recommendation:

The WCIRB initial recommendation of a 5.5 percent increase in the pure premium rate later amended to a recommendation for a 10.1 percent increase.

Insurance Commissioner approved:

A 10.1 percent increase effective January 1, 2001.

2002

WCIRB recommendation:

The WCIRB initial recommendation of a 9 percent increase in the pure premium rate later amended to a recommendation for a 10.2 percent increase.

WCIRB filed a mid-term recommendation that pure premium rates be increased by 10.1 percent effective July 1, 2002, for new and renewal policies with anniversary rating dates on or after July 1, 2002.

Insurance Commissioner approved:

A 10.2 percent increase effective January 1, 2002.

On May 20, 2002, the Insurance Commissioner approved a mid-term increase of 10.1 percent effective July 1, 2002.

2003

WCIRB recommendation:

The WCIRB initial recommendation of 11.9 percent was later amended. WCIRB filed a mid-term recommendation on April 2, 2003, that pure premium rates be increased by 10.6 percent effective July 1, 2003, for new and renewal policies with anniversary rating dates on or after July 1, 2003.

Insurance Commissioner Approved:

A 7.2 percent increase in pure premium rates applicable to new and renewal policies with anniversary rating dates on or after July 1, 2003.

**Advisory Workers' Compensation Pure Premium Rates
A History since the 1993 Reform Legislation
Part Three: 2004**

2004

WCIRB recommendation:

On July 30, 2003, WCIRB proposed an average increase in advisory pure premium rates of 12.0 percent to be effective on January 1, 2004, for new and renewal policies with anniversary rating dates on or after January 1, 2004.

The original WCIRB filing of an average increase of 12 percent on July 30, 2003, was later amended on September 29, 2003, to -2.9 percent to reflect the WCIRB's initial evaluation of AB 227 and SB 228.

In an amended filing made on November 3, 2003, the WCIRB recommended that pure premium rates be reduced, on average, from 2.9 percent to 5.3 percent.

On May 13, 2004, WCIRB proposed advisory pure premium rates that are approximately 13 percent to 15 percent less than the January 1, 2004, pure premium rates proposed by the WCIRB in its November 3, 2003, filing letter and represent a 2.9 percent decrease from the January 1, 2004, approved pure premium rates. These rates reflect the WCIRB's analysis of the impact of provisions of SB 899 on advisory pure premium rates.

On July 28, 2004, the WCIRB proposed advisory premium rates applicable to new and renewal policies with anniversary rating dates on or after January 1, 2005, that are, on average, 3.5 percent greater than the July 1, 2004, advisory pure premium rates approved by the insurance commissioner.

Insurance Commissioner Approved:

In a decision issued November 10, 2003, the Insurance Commissioner approved a total decrease of 14.9 percent in the workers' compensation pure premium rates that have been in effect since July 1, 2003. These rates will be applicable to new and renewal policies with anniversary rating dates on or after January 1, 2004.

In a decision issued May 28, 2004, the Insurance Commissioner approved a total decrease of 20.9 percent in the workers' compensation pure premium rate effective July 1, 2003, compared to a proposed 17.4 percent decrease filed by the WCIRB.

The Commissioner approved pure premium rates, effective July 1, 2004, with respect to new and renewal policies, reflecting a 7.0 percent decrease as compared to the approved January 1, 2004, pure premium rates.

In a decision issued November 17, 2004, the Insurance Commissioner approved a total 2.2 percent decrease in advisory pure premium rates applicable to new and renewal policies with anniversary rating dates on or after January 1, 2005.

Post-Reform WC Rate Filing Changes

As a result of recent workers' compensation legislative reforms and the subsequent decisions by the Insurance Commissioner (IC) on advisory premium rates, workers' compensation insurers have reduced their filed rates as indicated in the chart below.

The cumulative premium weighted average rate reduction filed is about 10 percent for those insurers that collectively have 80 percent of the market or 10.5 percent for all insurers. Broken down to account for Assembly Bill (AB) 227/Senate Bill (SB) 228 savings and SB 899 savings, filed rates were reduced 3.5 percent on January 1, 2004, and 7 percent on July 1, 2004.¹

However, actual final rates charged in the market were reduced by 7 to 8 percent during the first quarter of 2004, indicating that insurers discounted their filed rates by approximately 4 percent beyond the filed rate reduction of 3.5 percent.² This reduction did not yet reflect the savings resulting from SB 899 and the July 1, 2004, advisory pure premium rate reduction. Therefore, if the same level of market discounting continues through the third quarter of 2004 as was apparent during the first quarter of 2004, actual rates charged in the market could reasonably be expected to be lower than the 10.5 percent filed reductions by a similar magnitude of approximately 4 percent and will likely reflect actual market reductions of 14 percent to 15 percent.

California Workers' Compensation Insurance Carrier Rate Filing Changes in 2004

| COMPANY NAME | GROUP NAME | Market share 2003 | Cumulative % Change 1/1/04 to Present | 07/01/2004 % Filed Rate Change | 01/01/2004 % Filed Rate Change |
|--|------------------------|-------------------|---------------------------------------|--------------------------------|--------------------------------|
| STATE COMPENSATION INSURANCE FUND | | 53.07% | -9.70% | -7% | -2.9% |
| EVEREST NATIONAL INSURANCE COMPANY | Everest Re Group | 4.28% | -7.47% | -7% | -0.5% |
| ZENITH INSURANCE COMPANY | Zenith National Group | 3.66% | -10.00% | -10% | 0% |
| AMERICAN HOME ASSURANCE COMPANY | AIG Group | 2.43% | -10.72% | -7% | -4% |
| ZURICH AMERICAN INSURANCE COMPANY | Zurich Insurance Group | 1.65% | -17.47% | -10% | -8.3% |
| LIBERTY MUTUAL FIRE INSURANCE COMPANY | Liberty Mutual Group | 1.39% | -17.12% | -12.2% | -5.6% |
| HARBOR SPECIALTY INSURANCE COMPANY | Hanover Group | 1.36% | -7.00% | -7% | 0% |
| REPUBLIC INDEMNITY COMPANY OF CALIFORNIA | Great American Group | 1.30% | -20.86% | -7% | -14.9% |
| TRAVELERS CASUALTY AND SURETY COMPANY | Travelers Group | 1.29% | -14.60% | -14.6% | 0% |
| FEDERAL INSURANCE COMPANY | Chubb Group | 1.28% | -10.95% | -3% | -8.2% |

¹ Source: Douglas G. Barker, J.D., Bureau Chief, California Dept. of Insurance Rate Filing Bureau.

² Source: Dave Bellusci, Senior Vice President, Chief Actuary, California Workers' Compensation Insurance Rating Bureau (WCIRB).

Selected Indicators in Workers' Compensation: A Report Card for Californians

| COMPANY NAME | GROUP NAME | Market share 2003 | Cumulative % Change 1/1/04 to Present | 07/01/2004 % Filed Rate Change | 01/01/2004 % Filed Rate Change |
|---|------------------------|-------------------|---------------------------------------|--------------------------------|--------------------------------|
| NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PA | AIG Group | 1.24% | -10.72% | -7% | -4% |
| VIRGINIA SURETY COMPANY, INC. | Aon Corporation | 1.16% | -2.35% | -7% | 5% |
| COMMERCE AND INDUSTRY INSURANCE COMPANY | AIG Group | 1.10% | -10.72% | -7% | -4% |
| CLARENDON NATIONAL INSURANCE COMPANY | Hanover Group | 1.00% | -7.00% | -7% | 0% |
| ST. PAUL FIRE AND MARINE INSURANCE COMPANY | Travelers Group | 0.98% | -14.63% | -7% | -8.2% |
| MID-CENTURY INSURANCE COMPANY | Zurich Insurance Group | 0.96% | -13.60% | -10% | -4% |
| PREFERRED EMPLOYERS INSURANCE COMPANY | WR Berkley Group | 0.92% | -7.00% | -7% | 0% |

The recent workers' compensation rate filing changes noted above could be one of the signs that the workers' compensation insurance market is becoming more stable and competitive.

Workers' Compensation Earned Premium

WCIRB defines earned premium as the portion of a premium that has been earned by the insurer for policy coverage already provided. For example, one-half of the total premium will typically be earned six months into an annual policy term.

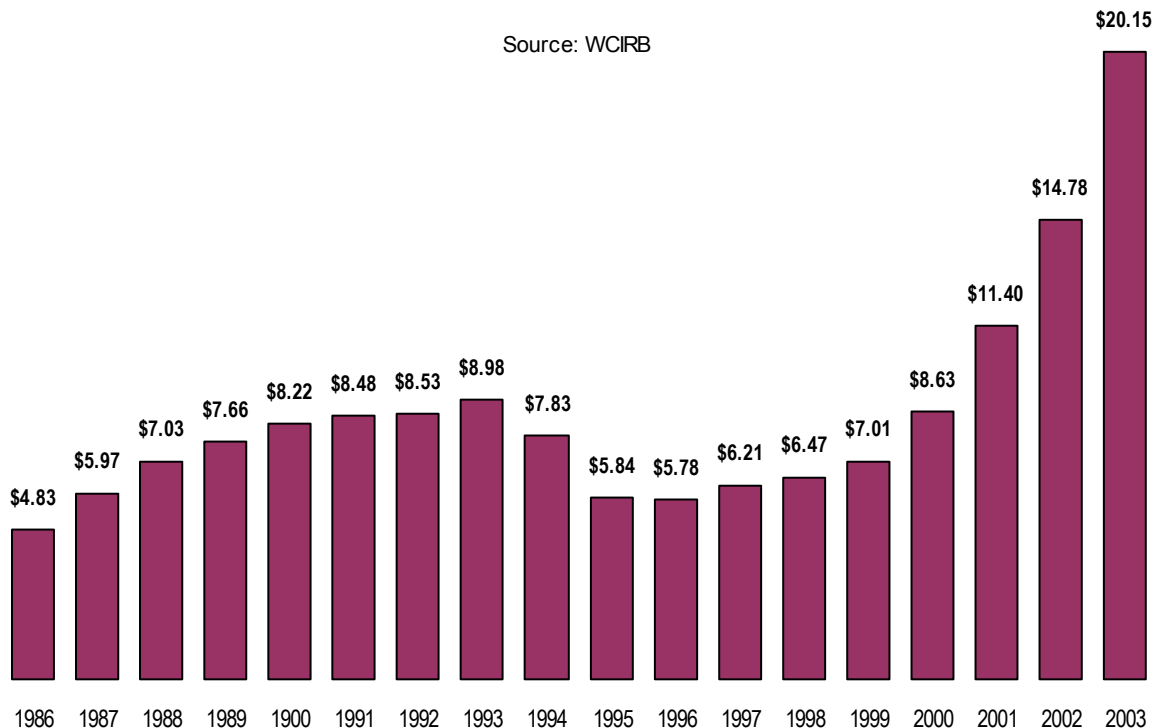
The total amount of earned workers' compensation premium decreased during the first half of the 1990's, increased slightly in the latter part of the decade, then increased sharply in the new millennium.

This increase in total premium appears to reflect:

- Movement from self-insurance to insurance.
- An increase in economic growth.
- Wage growth.
- Long-term movement from a manufacturing to a service economy.
- Increase in premium rates. Premiums in 2001 and 2002 were up sharply due primarily to rate increases in the market. The Workers' Compensation Insurance Rating Bureau (WCIRB) reports that the average rate on 2001 policies was about 34 percent higher than on 2000 policies and that the average rate on 2003 policies was 36 percent higher than on 2002 policies.

Workers' Compensation Earned Premium (in Billion\$)

Source: WCIRB

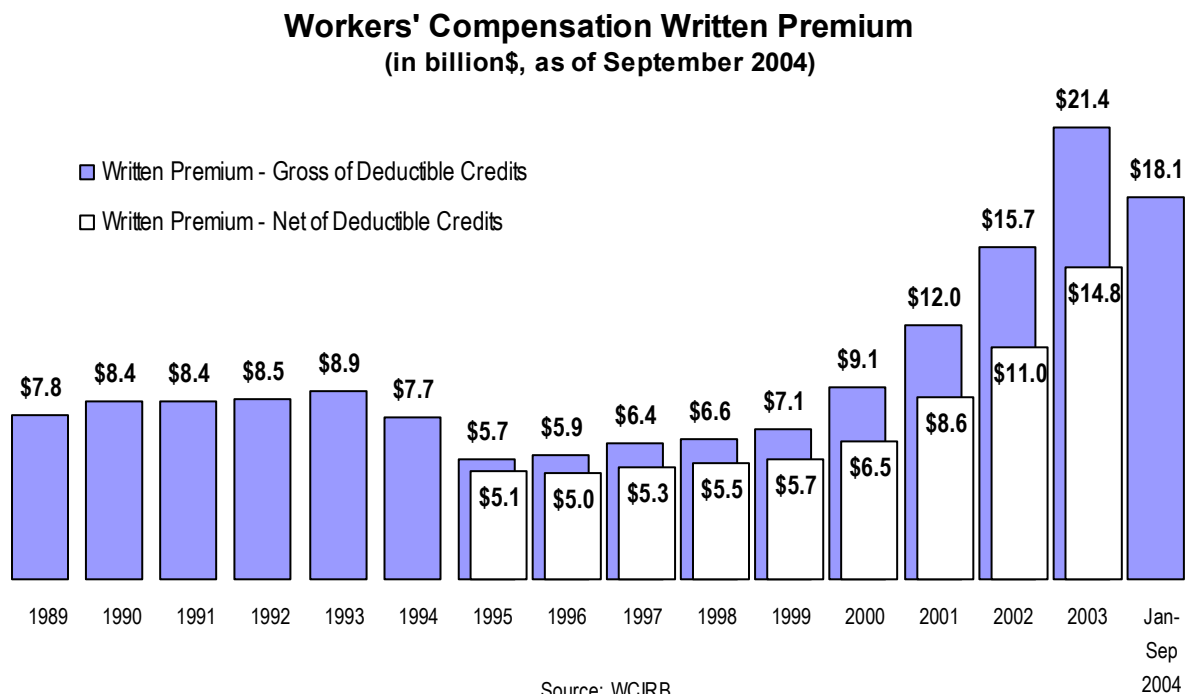


Workers Compensation Written Premium

California WC Written Premium

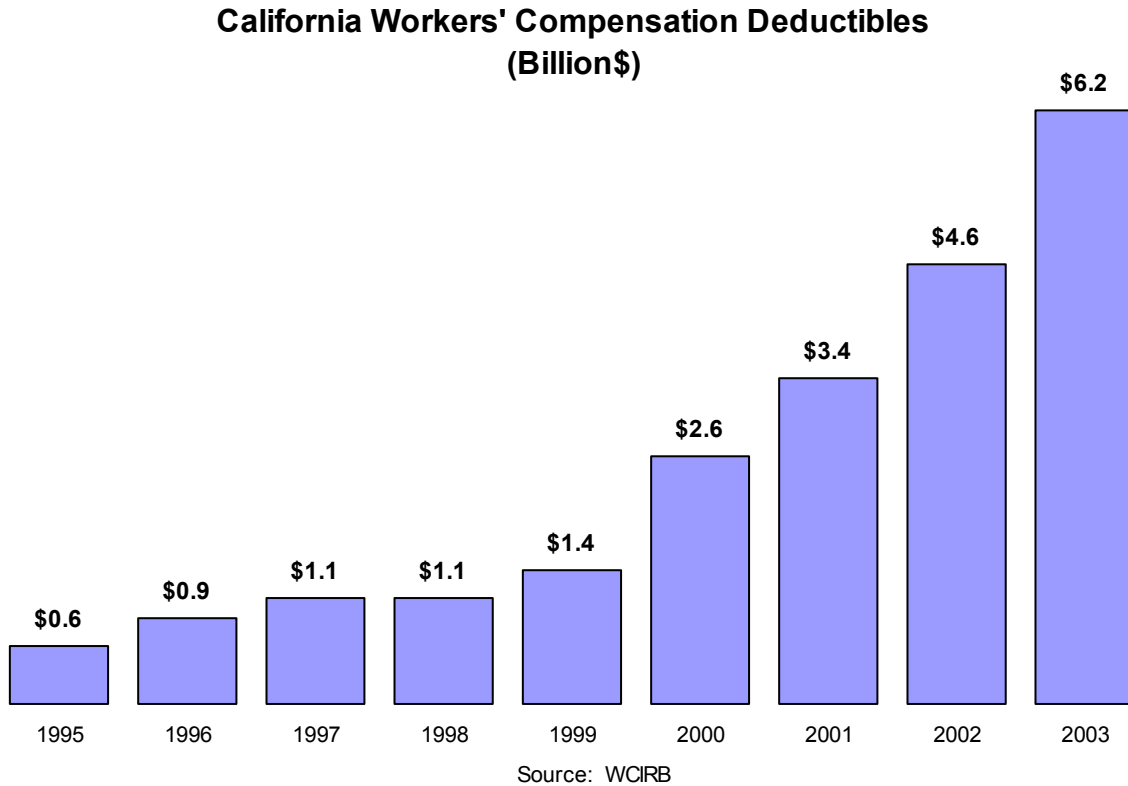
WCIRB defines written premium as the premium an insurer expects to earn over the policy period.

Workers' compensation premium decreased from 1993 to 1995, increased in the latter part of the decade, then increased sharply through 2003 and into 2004. This increase in written premium is primarily the result of rate increases over the past several years.



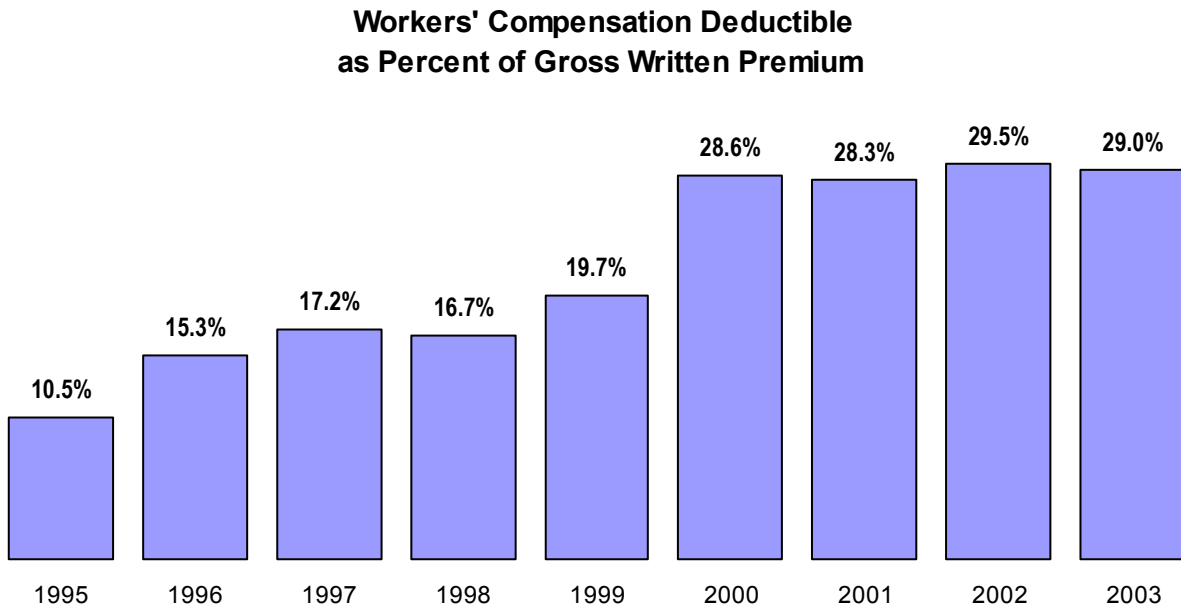
Workers' Compensation Deductibles

The following chart shows the changes in the total workers' compensation deductibles from 1995 to 2003.



WC Deductibles as Percent of Written Premium

The chart below shows workers' compensation deductibles as a percent of the written premium.

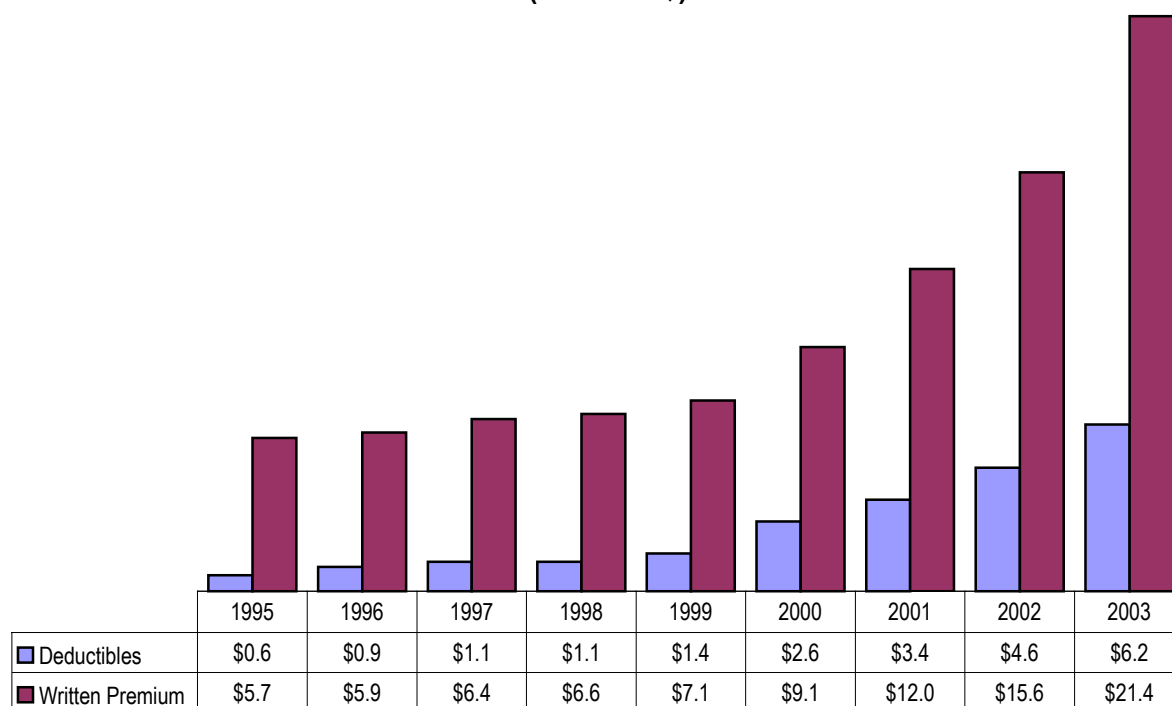


Source: WCRB

California WC Written Premium and Deductibles

The following chart compares the total workers' compensation written premium to the total deductibles from 1995 to 2003.

**Workers' Compensation Written Premiums and Deductibles
(in Billion\$)**

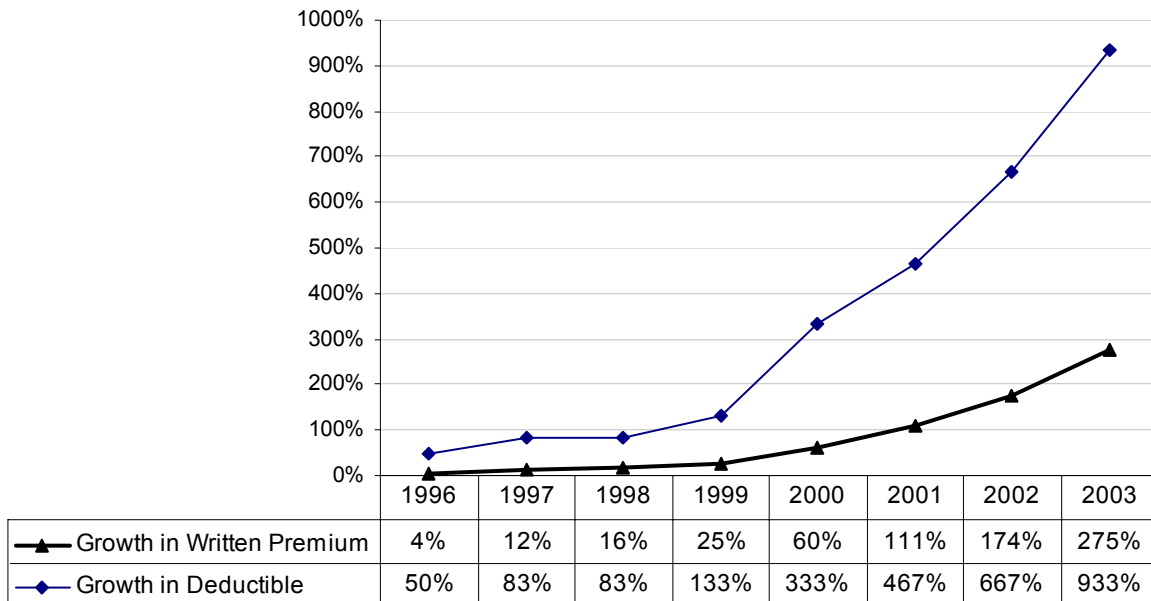


Source: WCIRB

Percentage Growth of Written Premium and Deductibles

The chart below shows the percentage growth of written premium and deductibles since 1995. Note that while written premium grew 274 percent, deductibles grew by 933 percent during the same time period, 1995 to 2003.

Percentage Growth of Written Premium and Deductibles Since 1995



Source: WCIRB

CALIFORNIA WORKERS' COMPENSATION INSURANCE INDUSTRY

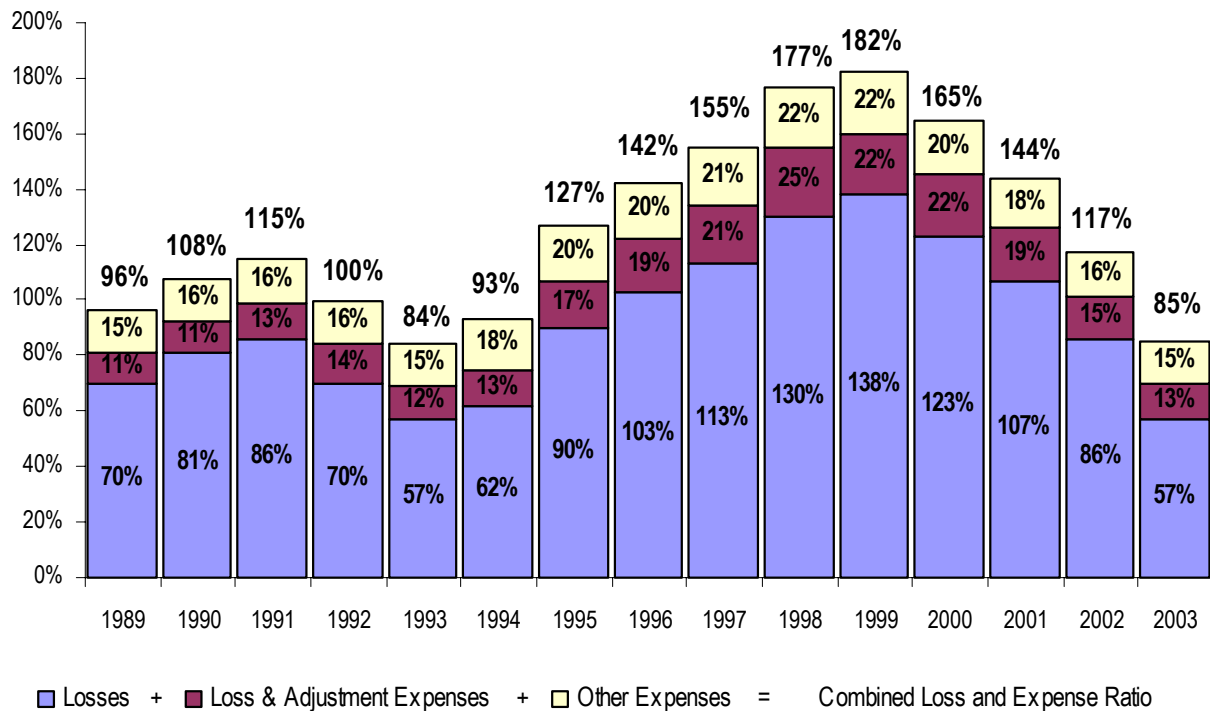
Workers' Compensation Insurer Expenses

Combined Loss and Expense Ratios

The accident-year combined loss and expense ratio, which measures workers' compensation claims payments and administrative expenses against earned premium, increased during the late 1990's and has been declining since that time. In accident-year 2003, insurers' claim costs and expenses amounted to \$0.85 for every dollar of premium they collected, which is the lowest combined ratio projected by WCIRB since the inception of competitive rating and reflects the estimated impact of AB 227 and SB 228 on unpaid medical losses.

WC Combined Loss and Expense Ratios

As of September 30, 2004
(After reflecting the estimated impact of
AB 277, SB 228 & SB 899 on unpaid losses)



Source: WCIRB

Under-reserving

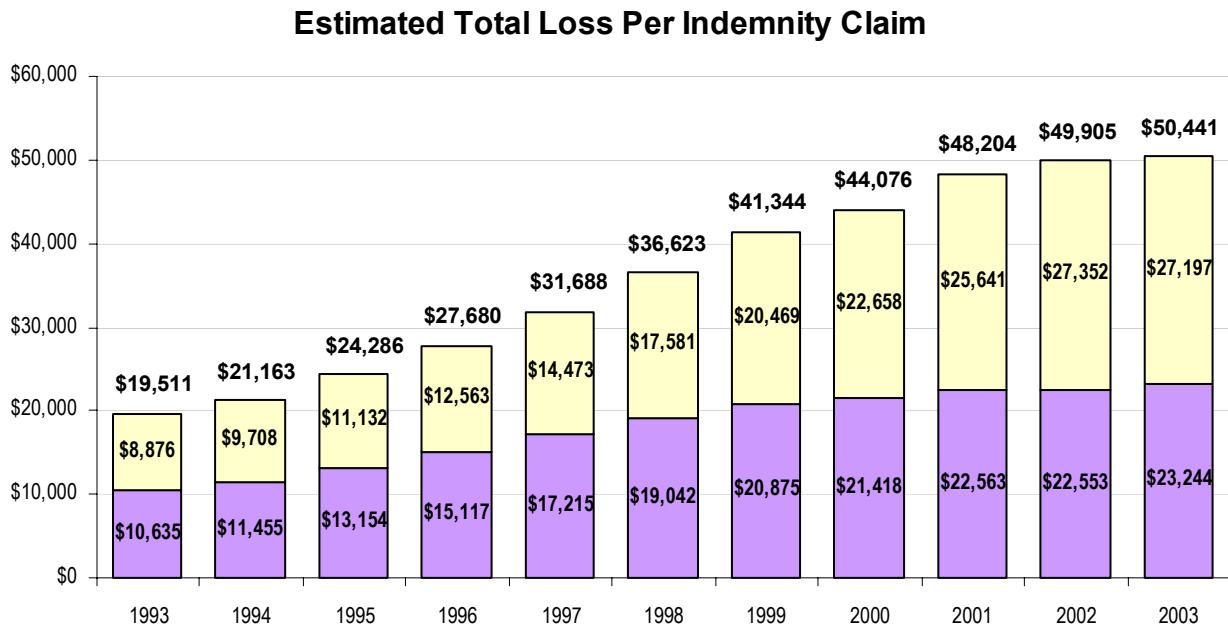
WCIRB estimates that the total cost of benefits on injuries occurring prior to January 1, 2004, exceeds insurer-reported loss amounts by \$7.1 billion. This figure, which may be symptomatic of reserve deficiencies for 2003, is down about 36 percent from 2002 and reflects the estimated impact of AB 227, SB 228, and SB 899 on unpaid losses.

According to WCIRB, a major factor has been the increase in medical costs during the late 1990's and early 2000's.

In addition, according to many members of the workers' compensation community, these results are also explained, at least in part, by inadequate pricing due to an extremely competitive insurance market. According to WCIRB, for most of the second half of the 1990's, insurers were, on average, pricing their policies well below the pure premium rate level. (Pure premium rates provide only for losses and loss-adjustment expenses and include no provision for other insurer expenses.)

Average Claim Costs

At the same time that premiums and claim frequency were declining, the total amount insurers paid on indemnity claims jumped sharply due to increases in the average cost of an indemnity claim, which rose dramatically during the late 1990's. According to WCIRB, both average indemnity and medical claim costs have shown increases over the past several years, as shown on the following graph.



Source: WCIRB

■ Estimated ultimate medical per indemnity claim +
■ Estimated ultimate indemnity per indemnity claim =
 Estimated Ultimate Total Losses per Indemnity Claim (excluding Medical-Only)

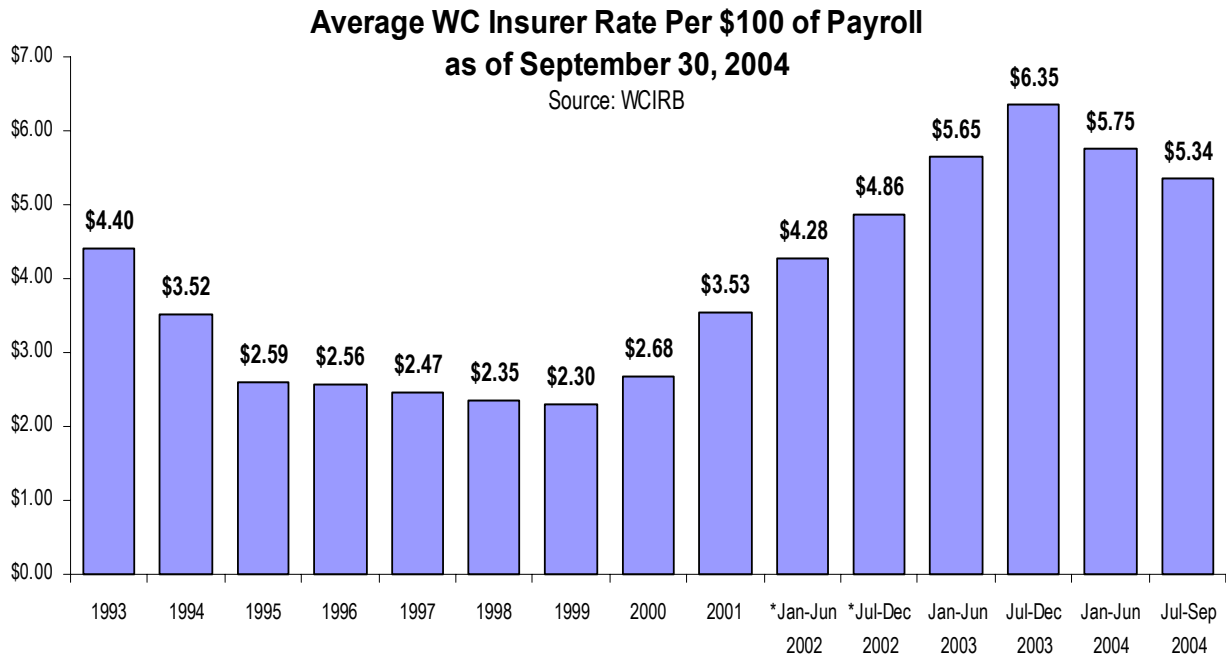
Please note that WCIRB's estimates of average indemnity claim costs have not been indexed to take into account wage increase and medical inflation.

WORKERS' COMPENSATION COSTS

Average California Workers' Compensation Premium Rate Per \$100 of Payroll

The following chart shows the average workers' compensation premium rate per \$100 of payroll. The average dropped during the early- to mid-1990's, stabilized during the mid- to late-1990's, and then rose significantly beginning in 2000.

However, the average statewide insurer rate per \$100 of payroll for policies written in the first quarter of 2004 was 8 percent below the average rate charged for the second six months of 2003. According to WCIRB, this rate was also 17 percent below the average rates that would have been charged in the first quarter of 2004 if average statewide rates had increased by the 12 percent increase in the advisory pure premium rates proposed by WCIRB prior to the enactment of AB 227, SB 228, and SB 899.

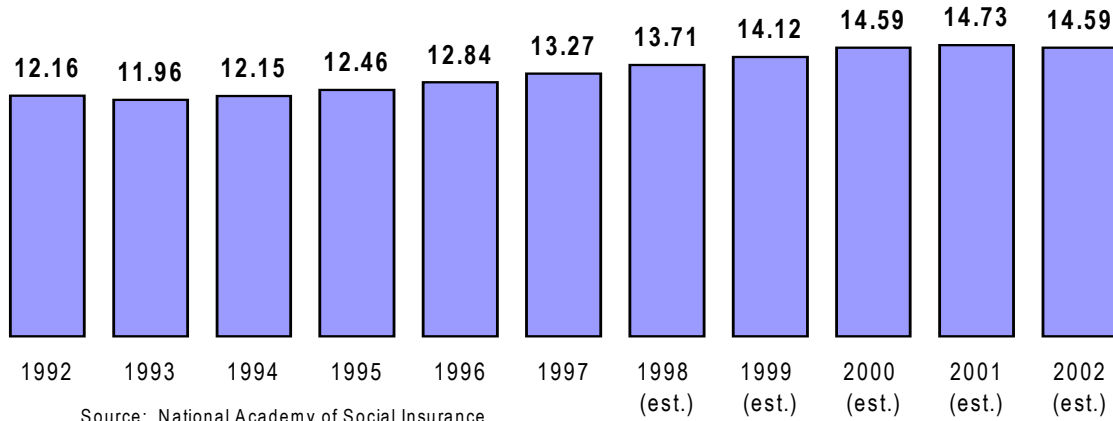


* Excludes the impact of the adopted changes to outstanding policy year 2002 pure premium rates effective January 1, 2003

Workers Covered by Workers' Compensation Insurance

Although the total earned premium increased from 1995, the number of workers covered by workers' compensation insurance also increased.

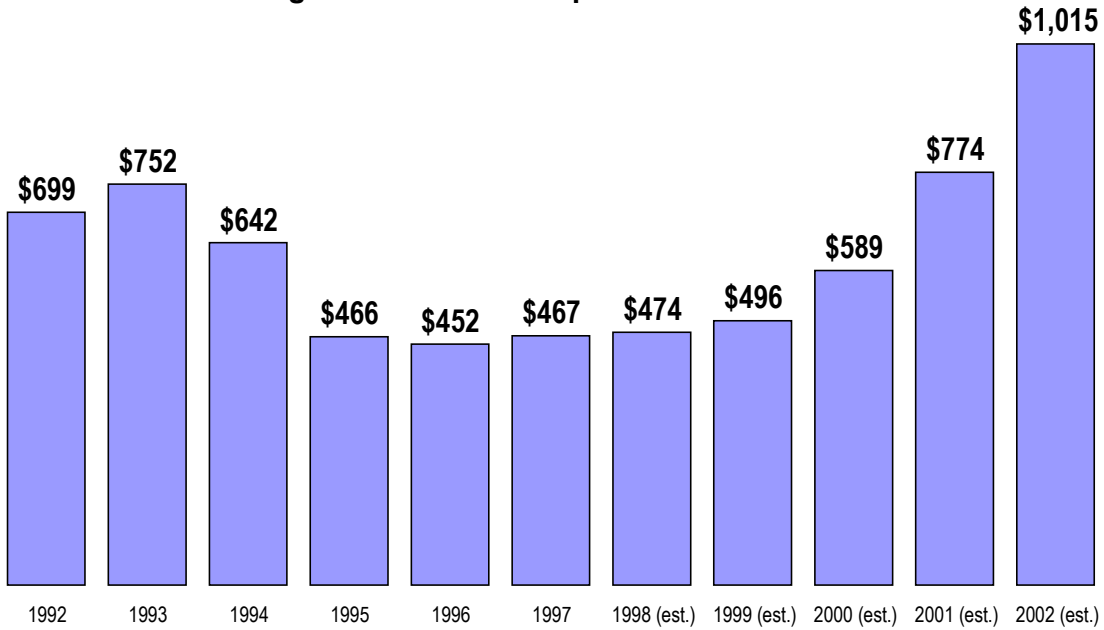
Workers Covered by Workers' Compensation Insurance (Millions)



Average Earned Premium per Covered Worker

As shown in the graph below, the average earned premium per covered worker dropped during the early- to mid-1990's, leveled off for a few years and then started to rise in 2000.

Average Earned Premium per Covered Worker



Data Sources: WCIRB and NASI
Calculations: CHSWC

Workers' Compensation Expenditures – Insured Employers

Indemnity Benefits

WCIRB provided the cost of indemnity benefits paid by insured employers. Assuming that insured employers comprise approximately 80 percent of all employers, estimated indemnity benefits are shown on the following chart for the total system and for self-insured employers as well.

System-wide Estimated Costs of Paid Indemnity Benefits

| Indemnity Benefit (Thousand\$) | 2002 | 2003 | Change |
|---------------------------------------|-------------|-------------|---------------|
| Temporary Disability | \$2,171,419 | \$2,498,083 | \$326,664 |
| Permanent Total Disability | \$75,608 | \$89,138 | \$13,530 |
| Permanent Partial Disability | \$2,037,250 | \$2,367,731 | \$330,481 |
| Death | \$58,073 | \$58,376 | \$304 |
| Funeral Expenses | \$2,125 | \$1,750 | -\$375 |
| Life Pensions | \$40,394 | \$41,535 | \$1,141 |
| Vocational Rehabilitation | \$618,155 | \$732,485 | \$114,330 |
| Total | \$5,003,023 | \$5,789,098 | \$786,075 |

Paid by Insured Employers

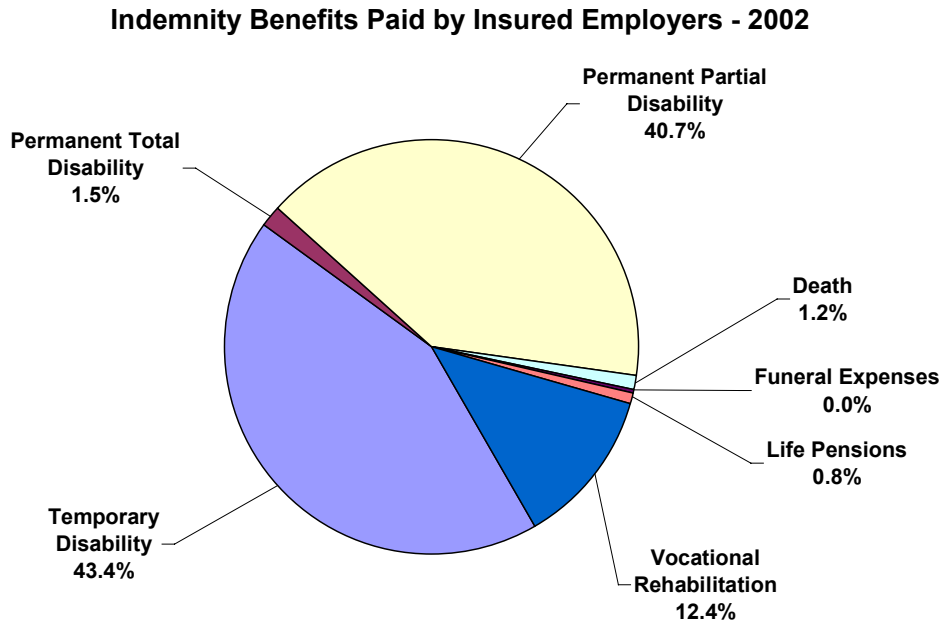
| Indemnity Benefit (Thousand\$) | 2002 | 2003 | Change |
|---------------------------------------|-------------|-------------|---------------|
| Temporary Disability | \$1,737,135 | \$1,998,466 | \$261,331 |
| Permanent Total Disability | \$60,486 | \$71,310 | \$10,824 |
| Permanent Partial Disability | \$1,629,800 | \$1,894,185 | \$264,385 |
| Death | \$46,458 | \$46,701 | \$243 |
| Funeral Expenses | \$1,700 | \$1,400 | -\$300 |
| Life Pensions | \$32,315 | \$33,228 | \$913 |
| Vocational Rehabilitation | \$494,524 | \$585,988 | \$91,464 |
| Total | \$4,002,418 | \$4,631,278 | \$628,860 |

Paid by Self-Insured Employers*

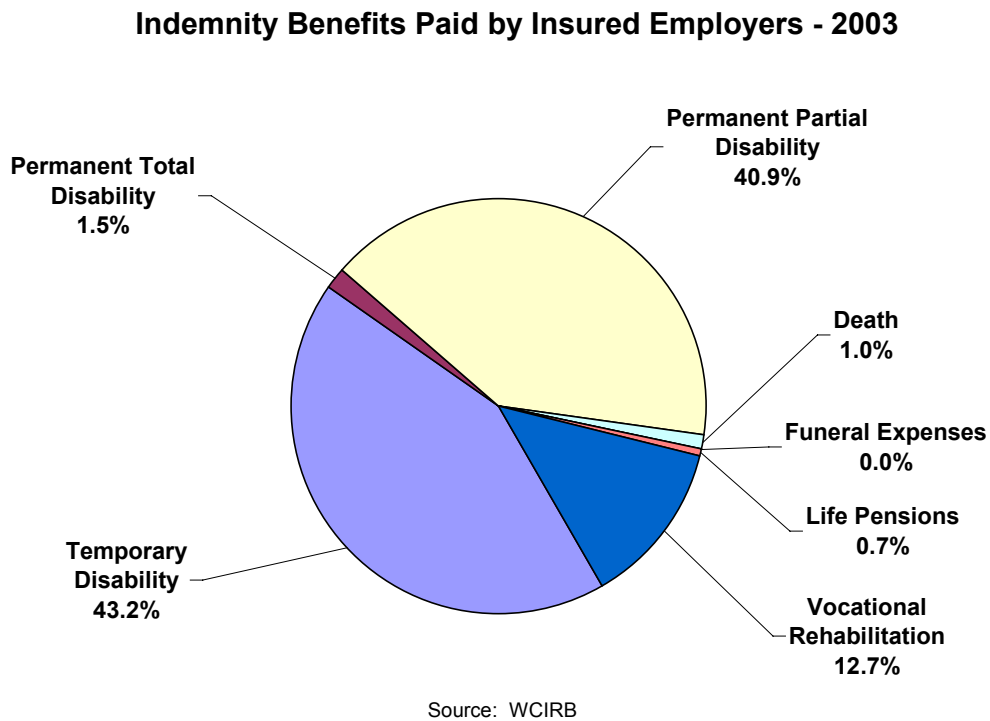
| Indemnity Benefit (Thousand\$) | 2002 | 2003 | Change |
|---------------------------------------|-------------|-------------|---------------|
| Temporary Disability | \$434,284 | \$499,617 | \$65,333 |
| Permanent Total Disability | \$15,122 | \$17,828 | \$2,706 |
| Permanent Partial Disability | \$407,450 | \$473,546 | \$66,096 |
| Death | \$11,615 | \$11,675 | \$61 |
| Funeral Expenses | \$425 | \$350 | -\$75 |
| Life Pensions | \$8,079 | \$8,307 | \$228 |
| Vocational Rehabilitation | \$123,631 | \$146,497 | \$22,866 |
| Total | \$1,000,605 | \$1,157,820 | \$157,215 |

The following shows the proportion of the types of indemnity benefits paid by insured employers. (Our method of estimating total system costs and self-insured costs based on insured employer costs would yield the same proportions for system-wide and self-insured.)

Indemnity Benefits Paid by Insured Employers – 2002



Indemnity Benefits Paid by Insured Employers – 2003



Medical Benefits

As reported by the WCIRB, workers' compensation medical benefits paid during 2003 by insured employers totaled \$4.9 billion, an increase from the \$4.1 billion paid in 2002.

System-Wide Estimated Costs - Medical Benefits Paid

| Medical Benefits (Thousand\$) | 2002 | 2003 Change | |
|--------------------------------------|--------------------|--------------------|------------------|
| Physicians | \$2,572,898 | \$3,207,516 | \$634,619 |
| Capitated Medical | \$7,710 | \$11,386 | \$3,676 |
| Hospital | \$1,409,135 | \$1,676,395 | \$267,260 |
| Pharmacy | \$370,774 | \$569,395 | \$198,621 |
| Payments Made Directly to Patient | \$297,428 | \$223,903 | -\$73,525 |
| Medical-Legal Evaluation | \$111,435 | \$160,429 | \$48,994 |
| Medical Cost Containment Programs* | \$356,781 | \$243,709 | -\$113,073 |
| Total | \$5,126,160 | \$6,092,733 | \$966,573 |

Paid by Insured Employers

| Medical Benefits (Thousand\$) | 2002 | 2003 Change | |
|--------------------------------------|--------------------|--------------------|------------------|
| Physicians | \$2,058,318 | \$2,566,013 | \$507,695 |
| Capitated Medical | \$6,168 | \$9,109 | \$2,941 |
| Hospital | \$1,127,308 | \$1,341,116 | \$213,808 |
| Pharmacy | \$296,619 | \$455,516 | \$158,897 |
| Payments Made Directly to Patient | \$237,942 | \$179,122 | -\$58,820 |
| Medical-Legal Evaluation | \$89,148 | \$128,343 | \$39,195 |
| Medical Cost-Containment Programs* | \$285,425 | \$194,967 | -\$90,458 |
| Total | \$4,100,928 | \$4,874,186 | \$773,258 |

Paid by Self-insured Employers**

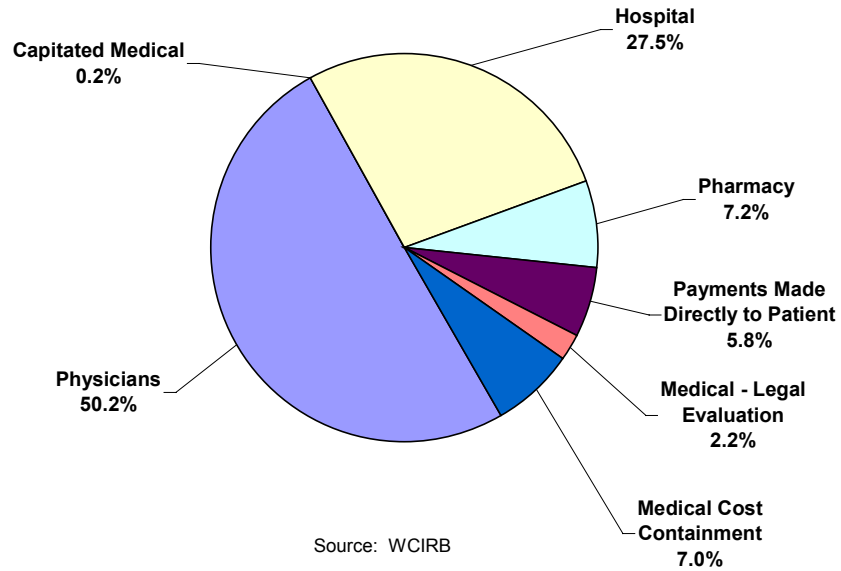
| Medical Benefits (Thousand\$) | 2002 | 2003 Change | |
|--------------------------------------|--------------------|--------------------|------------------|
| Physicians | \$514,580 | \$641,503 | \$126,924 |
| Capitated Medical | \$1,542 | \$2,277 | \$735 |
| Hospital | \$281,827 | \$335,279 | \$53,452 |
| Pharmacy | \$74,155 | \$113,879 | \$39,724 |
| Payments Made Directly to Patient | \$59,486 | \$44,781 | -\$14,705 |
| Medical-Legal Evaluation | \$22,287 | \$32,086 | \$9,799 |
| Medical Cost-Containment Programs* | \$71,356 | \$48,742 | -\$22,615 |
| Total | \$1,025,232 | \$1,218,547 | \$193,315 |

* Figures for medical cost-containment programs are based on a sample of insurers who reported medical cost-containment expenses to WCIRB.

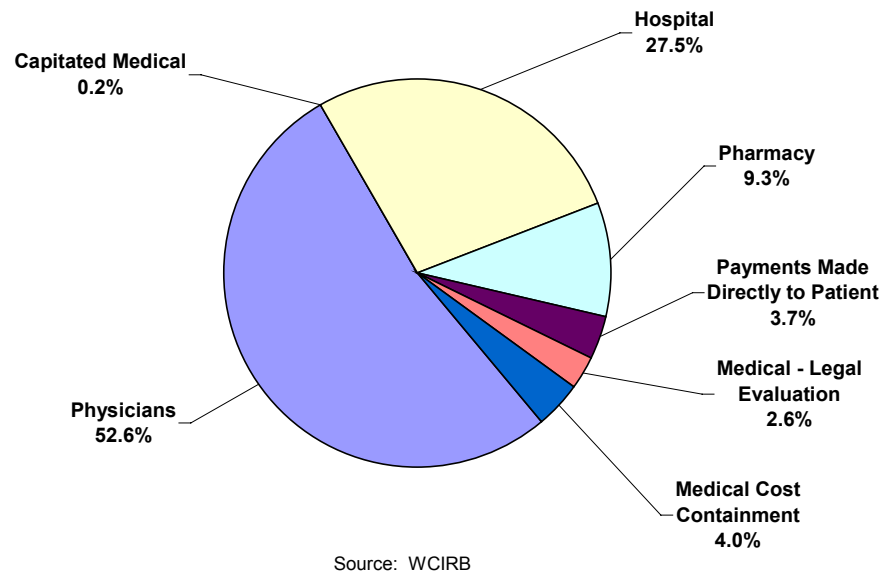
** Figures estimated based on insured employers' costs.

Self-insured employers are estimated to comprise 20 percent of all California employers.

Medical Benefits Paid by Insured Employers 2002



Medical Benefits Paid by Insured Employers - 2003



Average Cost per Claim by Type of Injury

As shown in the following chart, there have been significant increases in average cost per claim for several types of injury. From 1997 to 2003, slips and falls increased by 61 percent, back injuries by 59 percent, followed by carpal tunnel/repetitive motion injuries by 56 percent. On the other hand, average costs of psychiatric and mental stress claims appeared to level off until 2001, then increased slightly in 2002, and decreased slightly in 2003.

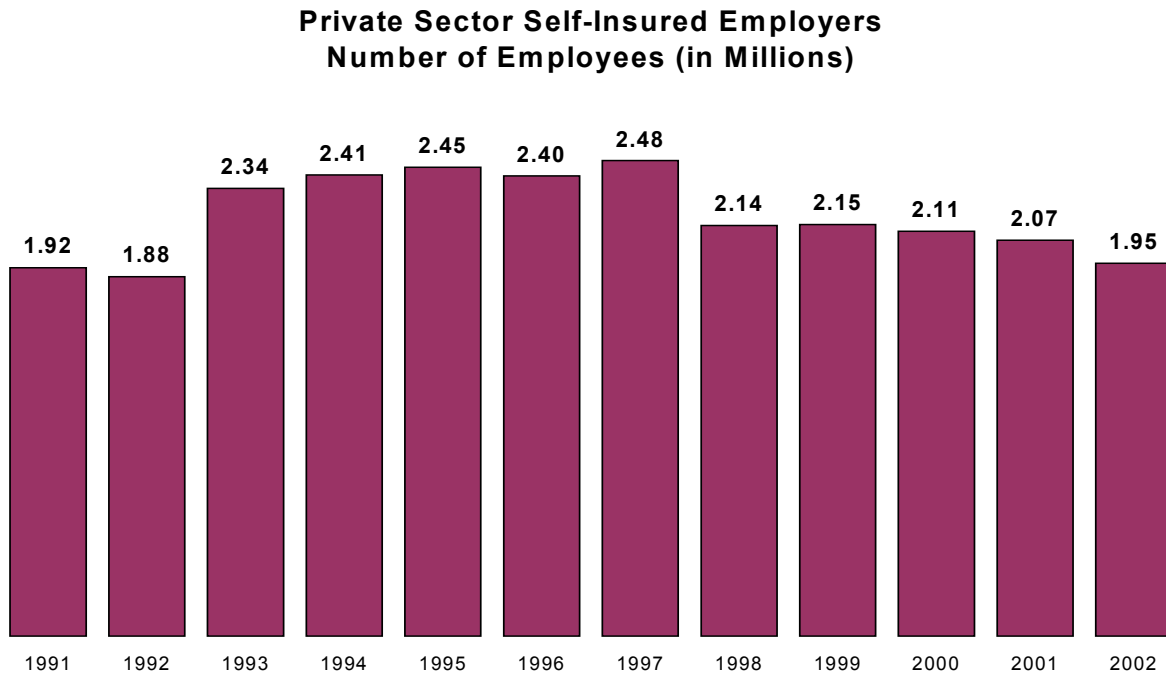
Average Cost per WC Claim by Type of Injury*



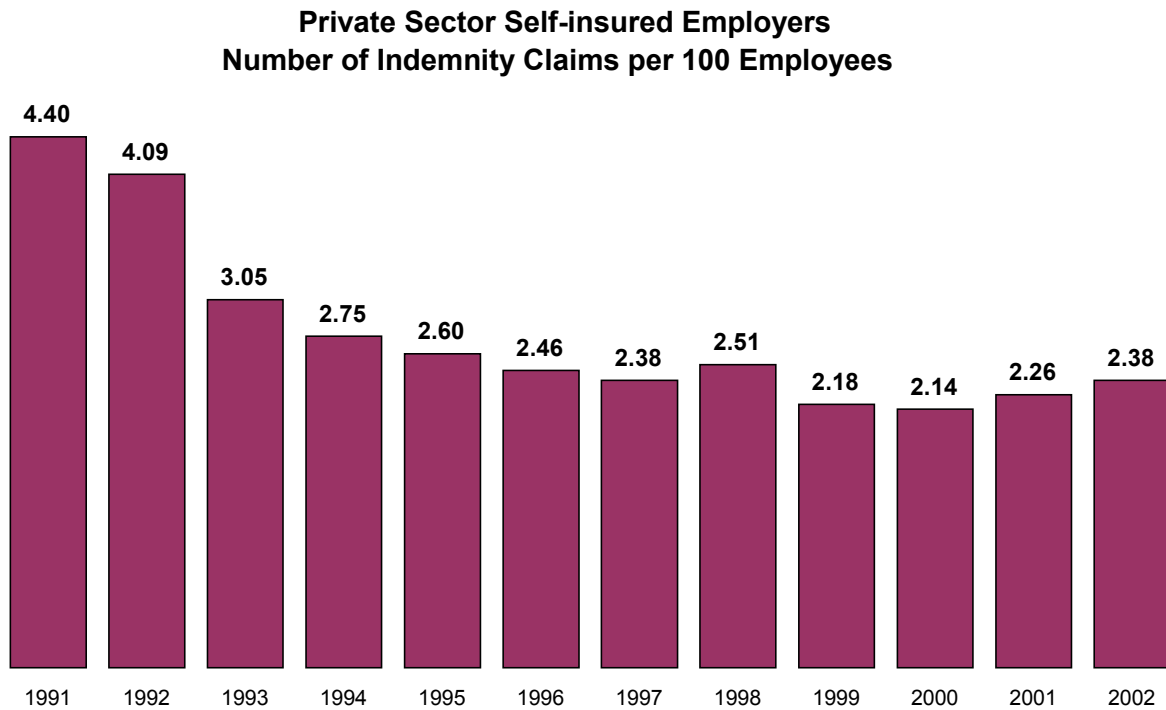
* These categories are not mutually exclusive. For example, some back injuries result from slips and falls.

Source: WCIRB

Workers' Compensation Expenditures - Private Sector Self-insured Employers

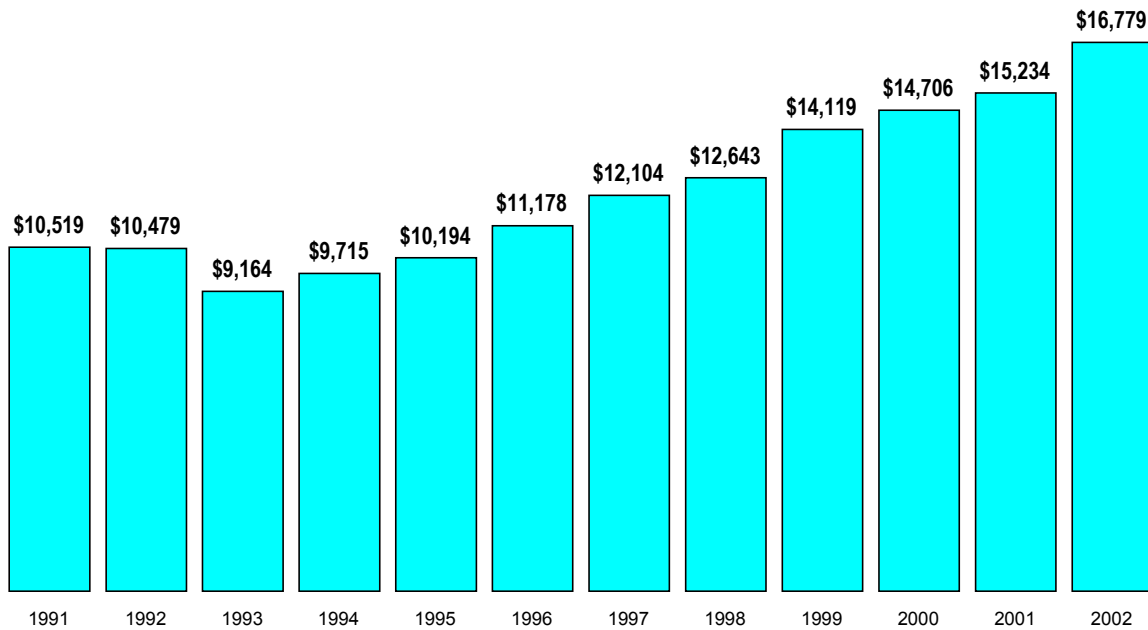


Source: DIR Self-Insurance Plans



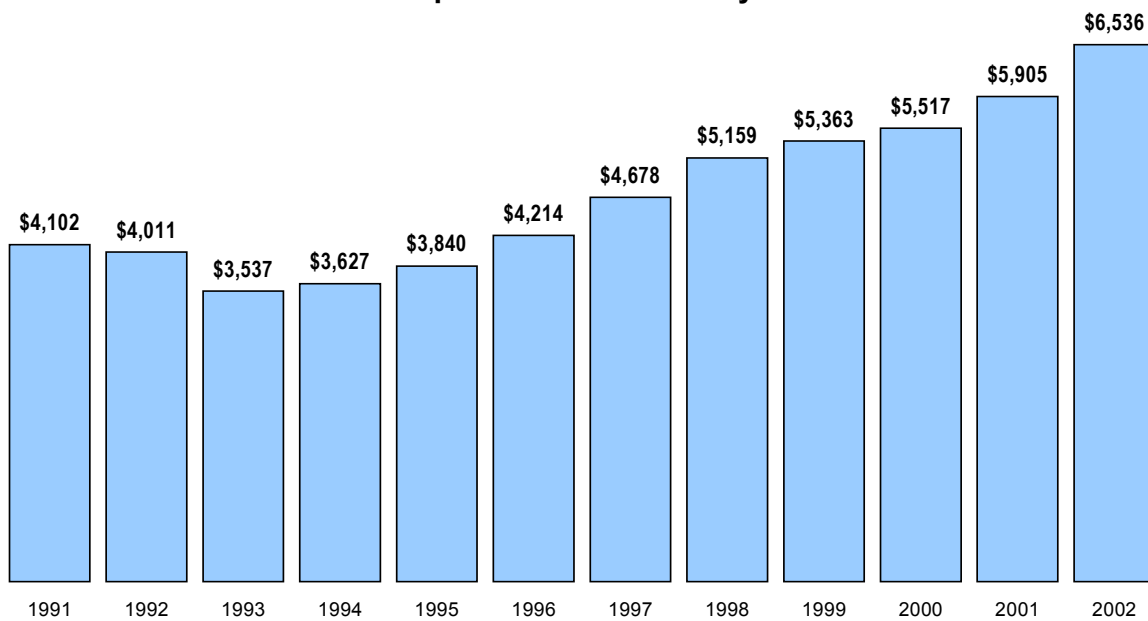
Source: DIR Self-Insurance Plans

**Private Sector Self-insured Employers
Incurred Cost per Indemnity Claim**



Source: DIR Self-Insurance Plans

**Private Sector Self-Insured Employers
Incurred Cost per Claim - Indemnity and Medical**

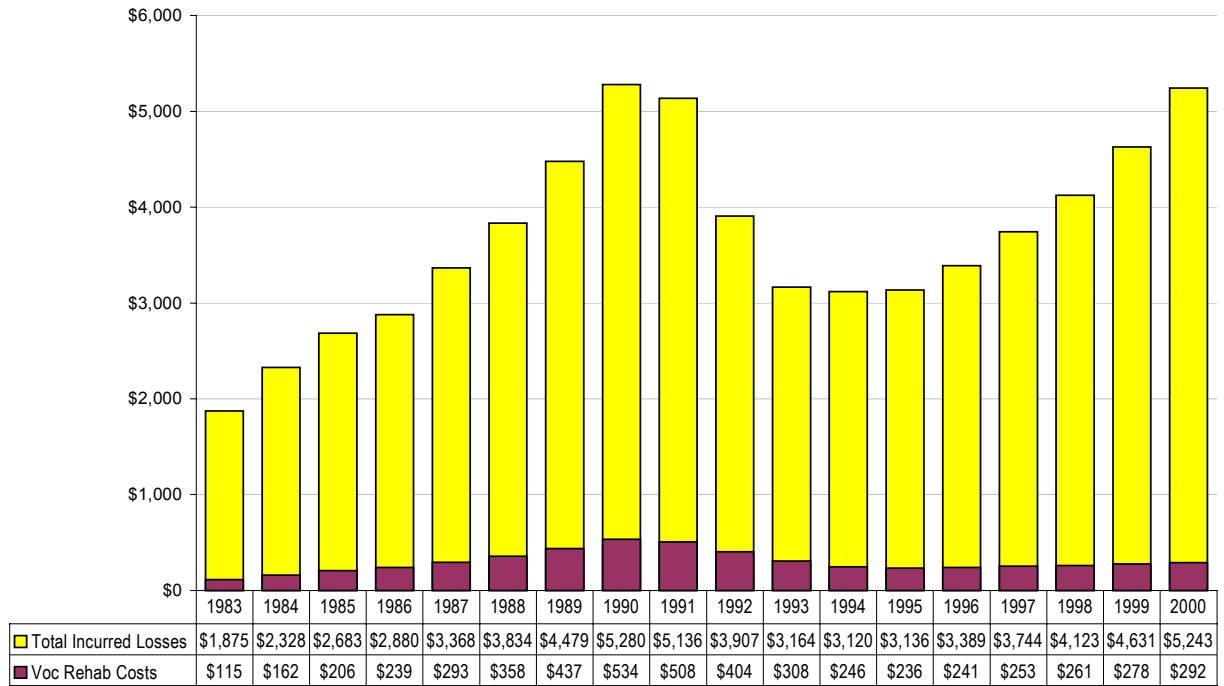


Source: DIR Self-Insurance Plans

Vocational Rehabilitation Costs

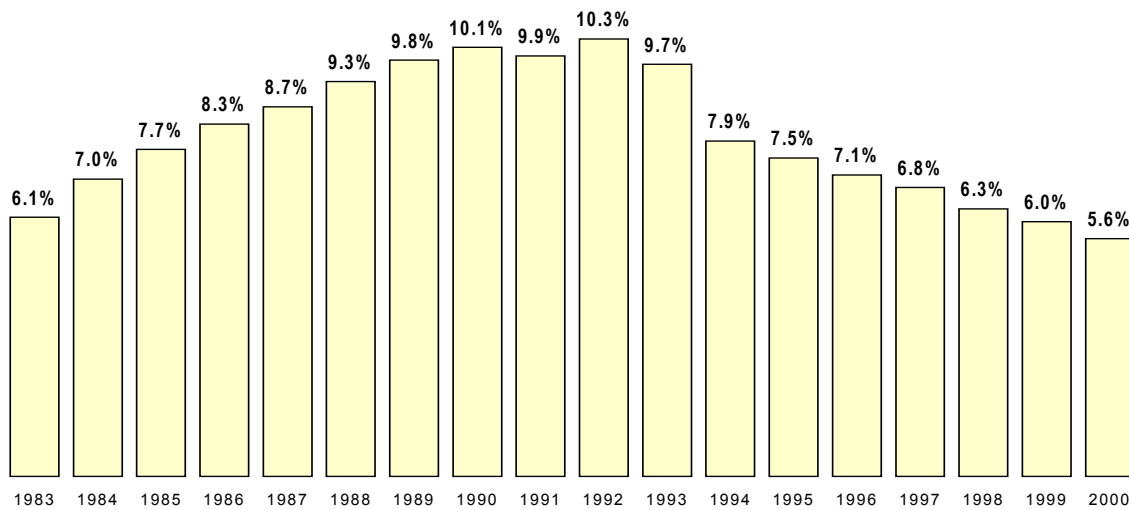
Total workers' compensation vocational rehabilitation costs rose from policy-year 1983 to 1990, then declined thereafter, slightly increasing in 1999 and returning to the 1990 level in 2000. Total incurred losses peaked in 1990, declined to 1995, and then increased again through 2000.

Vocational Rehabilitation Costs compared with Total Incurred Losses (in Million\$)



Source: WCIRB

Vocational Rehabilitation Costs as Percent of Total Incurred Losses



Source: WCIRB

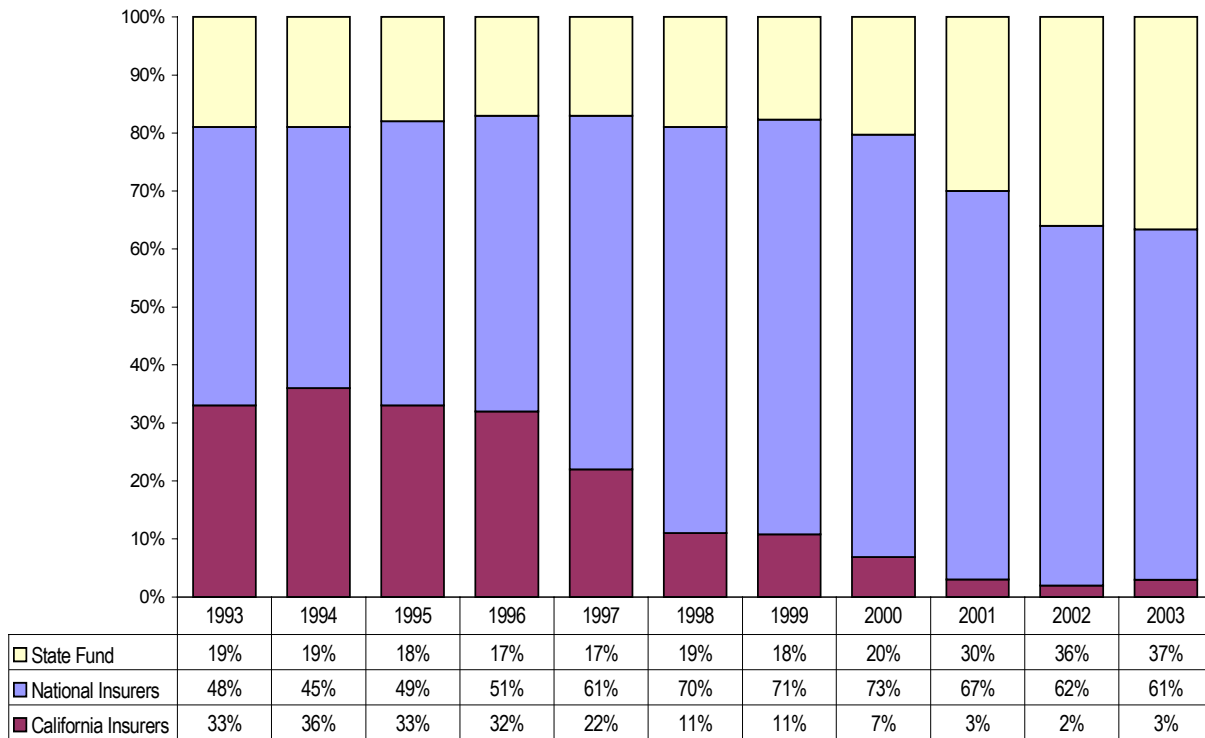
Current State of the Insurance Industry

Market Share

A number of California insurers left the market or reduced their writings as a result of the decrease in profitability, contributing to a major redistribution of market share among insurers since 1993, as shown in the following chart.

According to WCIRB, California companies (excluding SCIF) insured just 3 percent of the California workers' compensation market in 2003, compared with 36 percent of the market in 1994. In 2003, SCIF attained 37 percent of the California workers' compensation insurance market, double the market share it had in the 1990's.

**California Workers' Compensation Insurance Market Share
By Type of Insurer 1993-2003**



Source: WCIRB

Please note that totals may not equal 100% due to rounding.

"September 11" Impact on Insurance Industry

The recent problems in the reinsurance market caused by the events of September 11, 2001, have significantly affected the cost and availability of catastrophe reinsurance and, correspondingly, have a significant effect on the cost of workers' compensation insurance. This extends to more than acts of terrorism and is a critical component of any evaluation of the California workers' compensation insurance marketplace.

INSURANCE MARKET INSOLVENCY

CIGA Assessments and Deductibles

As described above, CIGA receives a significant amount of its funding through imposing a 2 percent assessment. This assessment is made against the “net direct written premium” of the workers’ compensation carriers. There is a precedent for assessing against the entire gross written premium before the application of the large deductible discounts, namely, the Worker’s Compensation Insurance Rating Bureau (WCIRB) for its operating expenses, and the Division of Workers’ Compensation (DWC) for its Workers’ Compensation Administrative Revolving Fund (WCARF). In addition, several states are also assessing against the “net direct written premium to cover the CIGA fund.”

In addition, the self-insureds pay 2 percent of the benefits paid on claims incurred during the previous year to make up the deficit for defaulted self-insured employers’ liabilities pursuant to Labor Code Section 3745(b). Also, most of the self-insured employers participate in the alternative security deposit provided by the Security Fund and are paying a deposit assessment to the Fund, which is determined based on their required deposit amount and their credit worthiness. Some members of the workers’ compensation community have expressed concern that since the use of large deductibles by medium and large employers has steadily grown in California since they were introduced in 1995, small employers are indirectly paying a disproportionate amount of the CIGA assessment.

Currently, several insurance companies are experiencing problems with payment of claims.

As indicated in the following listing, over 20 insurance companies have gone under liquidation since 2000.

COMPANY NAME

DATE OF LIQUIDATION

2000

| | |
|--|------------|
| California Compensation Insurance Company | 9/26/2000 |
| Combined Benefits Insurance Company | 9/26/2000 |
| Commercial Compensation Casualty Insurance Company | 9/26/2000 |
| Credit General Indemnity Company | 12/12/2000 |
| LMI Insurance Company | 5/23/2000 |
| Superior National Insurance Company | 9/26/2000 |
| Superior Pacific Insurance Company | 9/26/2000 |

2001

| | |
|--|-----------|
| Credit General Insurance Company | 1/5/2001 |
| Great States Insurance Company | 5/8/2001 |
| HIH America Compensation & Liability Insurance Company | 5/8/2001 |
| Amwest Surety Insurance Company | 6/7/2001 |
| Sable Insurance Company | 7/17/2001 |

Selected Indicators in Workers' Compensation: A Report Card for Californians

| | |
|------------------------------------|------------|
| Reliance Insurance Company | 10/3/2001 |
| Far West Insurance Company | 11/9/2001 |
| Frontier Pacific Insurance Company | 11/30/2001 |

2002

| | |
|--|-----------|
| PHICO | 2/1/2002 |
| National Auto Casualty Insurance Company | 4/23/2002 |
| Paula Insurance Company | 6/21/2002 |
| Alistar Insurance Company | 11/2/2002 |
| Consolidated Freightways | 9/2002 |

2003

| | |
|--|-----------|
| Western Growers Insurance Company | 1/7/2003 |
| Legion Insurance Company | 3/25/2003 |
| Villanova Insurance Company | 3/25/2003 |
| Home Insurance Company | 6/13/2003 |
| Fremont General Corporation | 7/2/2003 |
| Wasatch Crest Insurance Co. (No WC policies) | 7/31/2003 |
| Pacific National Insurance Co. | 8/5/2003 |

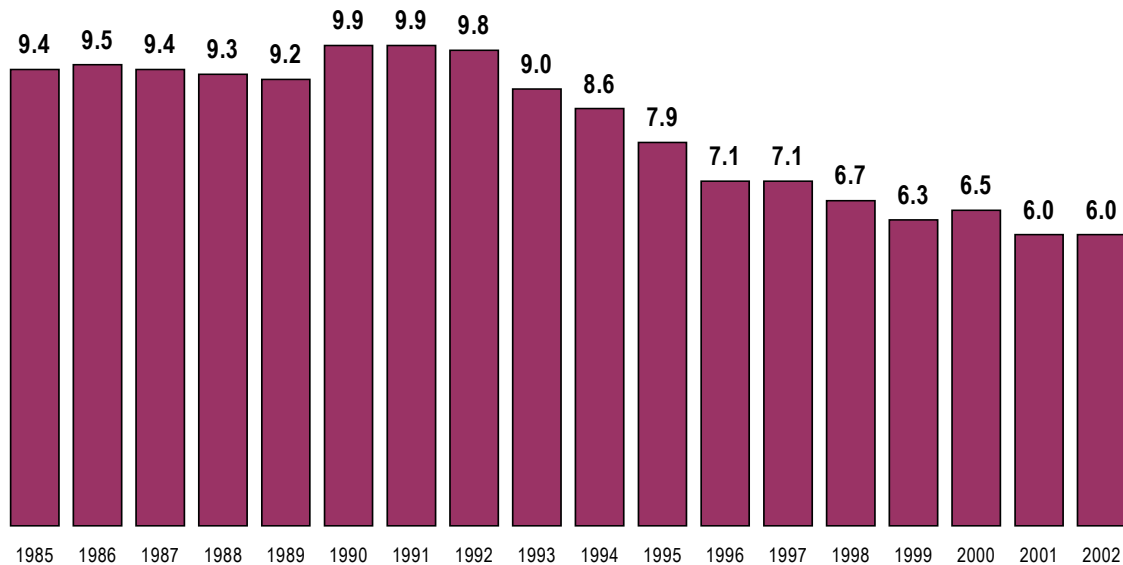
Injuries and Illnesses

Non-fatal Injury and Illness Rates in California

From 1990 to 2002, the injury and illness rates in California declined from a high of 9.9 cases per 100 employees in 1990 and 1991 to 6.0 cases per 100 employees in 2002.

This improvement has been attributed to a number of factors, including shifts in the workforce, greater emphasis on workplace safety, continued efforts to combat workers' compensation fraud, and changes in employer reporting patterns.

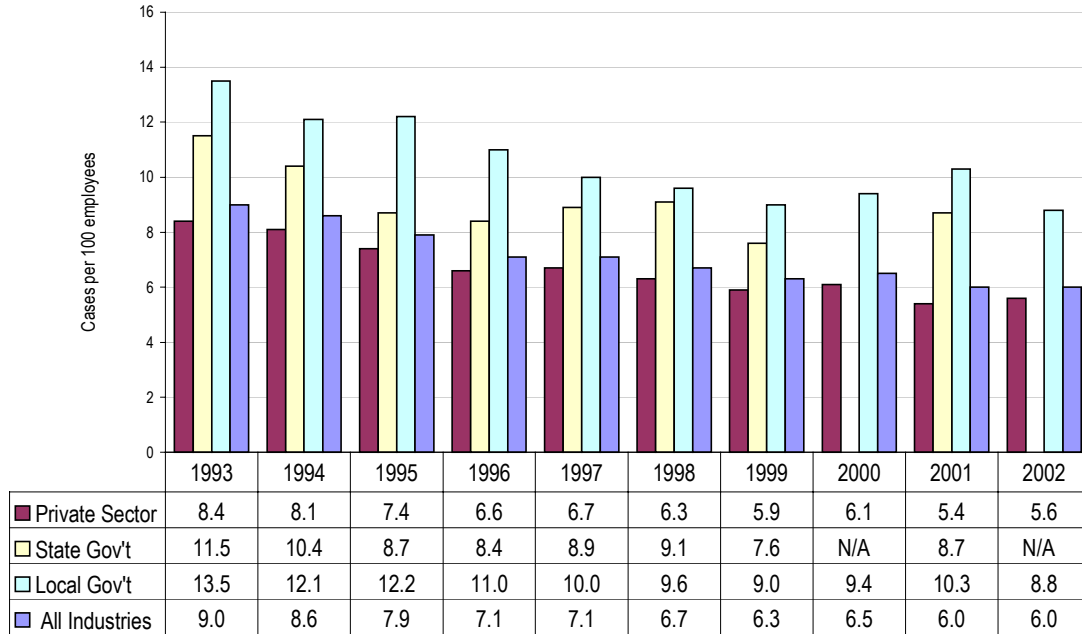
OSHA Injury and Illness Rates in California 1985-2002
(Cases per 100 employees)



Source: Division of Labor Statistics and Research (DLSR)

As shown on the following chart, the injury and illness rates for the public and private sectors are also declining.

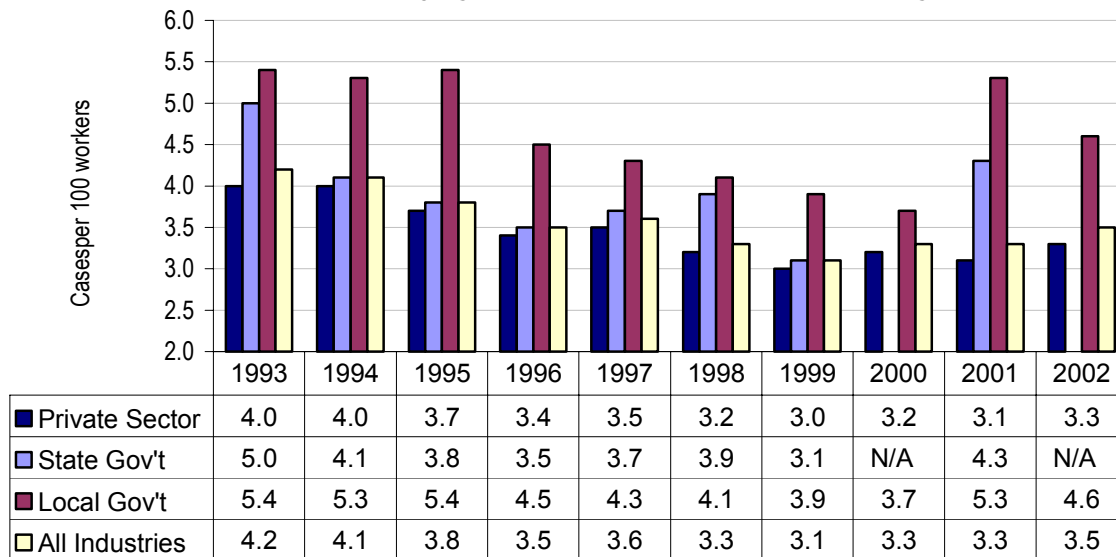
Occupational Injury and Illness Rates in California by Sector



Source: Division of Labor Statistics and Research (DLSR)

Lost-time injury rates have declined from 1993 to 1999 and have started to increase since 2000, especially in the public sectors.

Lost Time Injury and Illness Rates in California by Sector

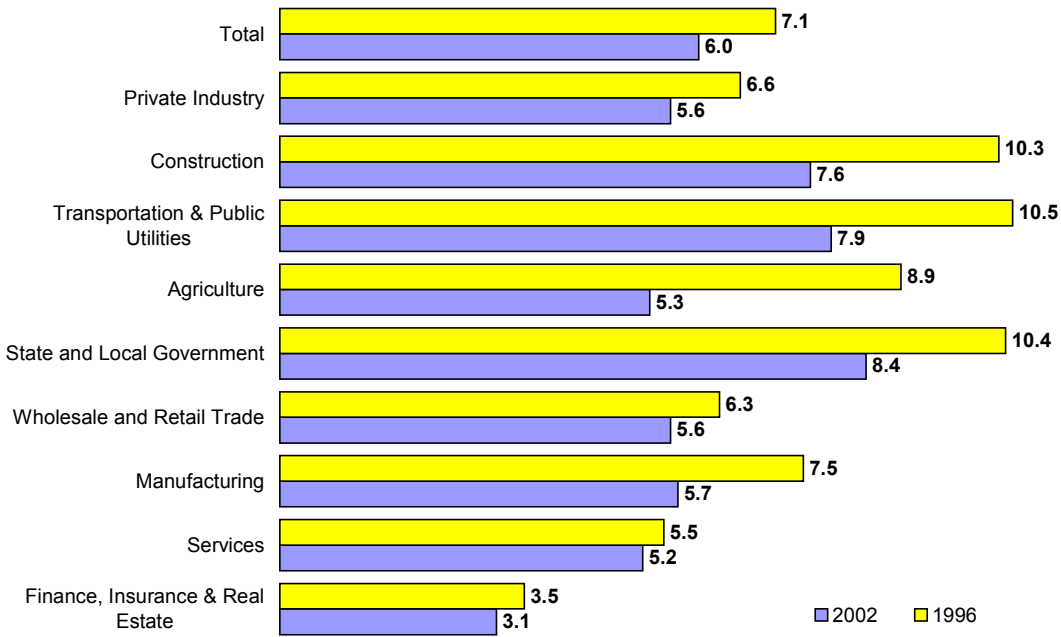


Source: Division of Labor Statistics and Research

Non-fatal Occupational Injuries and Illness Days-away-from-work Rates by Industry

Injury and illness days-away-from-work rates in all industries declined between 1996 and 2002.

Injury Rates by Industry 2002 v 1996



Source: Division of Labor Statistics and Research

Profile of Injury and Illness Statistics

Data for the following analyses, except where noted, were derived from the Department of Industrial Relations (DIR) Division of Labor Statistics and Research (DLSR), from the United States Department of Labor (DOL) Bureau of Labor Statistics (BLS) and from the California Workers' Compensation Institute (CWCI).

California and the Nation

Incidence Rates

California's most recent work injury and illness statistics (2002) indicate an injury and illness rate of 5.6 cases per 100 full-time employees in the private sector in 2002. This is a 40 percent decline from the 1990 peak level of 9.4 and an estimated 4 percent increase from the previous year's figures.

The above trend in California mirrors a national trend. DOL figures for private employers show that from 1990 to 2002, the work injury and illness rate across the U.S. fell from 8.8 to 5.3 cases per 100 employees in the private sector. The reduction in the number of incidences of job injuries is likely due to various factors including a greater emphasis on job safety, the improving economy since the early 1990's, and the shift from manufacturing toward service jobs.

From the Western region states (Alaska, Arizona, California, Hawaii, Nevada, Oregon and Washington), California's 2002 private-industry rate of 5.6 for non-occupational injuries and illnesses is the second lowest.³ The state with the lowest incidence rate of 5.0 in 2002 was Arizona.

Duration

Days-away-from-work cases, including those that result in days away from work with or without a job transfer or restriction, dropped from 2.1 to 1.8 cases per 100 full-time employees from 1996 to 2002 in the private sector. This also mirrors the national trend with the number of cases of days away from work falling from 2.2 to 1.6 cases in the national private sector with a similar decline as that of California.

In "State Report Cards for Workers' Compensation," published by the Work-Loss Data Institute, the Institute reported that the median days away from work in California and New York is 8 days, compared with the national average of 6 days.⁴

Industry Data

- In 2002, injury and illness incidence rates varied greatly between private industries ranging from 3.1 injuries/illnesses per 100 full-time workers in finance, insurance and real estate to 7.9 in transportation and public utilities. California's private industry rates for total cases were higher than the national rates in every major industry division, except for manufacturing and agriculture, forestry and fishing.

³ The comparisons of industry rates have not been adjusted for industry mix within each state.

⁴ http://www.odg-disability.com/pr_repsrc.htm

- While the private industry total case rate increased between 2001 and 2002, the rate for the public sector (state and local government) decreased 15 percent from 9.9 in 2001 to 8.4 in 2002.
- Over the past decade (1992-2002), the number of fatal injuries declined by about 27 percent, from 651 to 478. The number of fatal injuries declined by 25 percent since 1996. The number of fatal injuries decreased by 6 percent from 2001 to 2002. Injuries continued to decline in 2003 to 456 fatalities. The highest number of fatal injuries was in trade, transportation and utilities, closely followed by construction.
- In private industry, the top five occupations with the most non-fatal injuries and illnesses in descending order are: truck drivers, laborers (non-construction), janitors and cleaners, carpenters, and nursing aides, orderlies and attendants.
- Truck drivers, construction laborers, farm workers, ground maintenance workers and police officers were the occupations with the most number of fatal injuries in 2003. Transportation accidents were the number one cause of fatal injuries accounting for about 38 percent of fatal injuries in 2003.
- Assaults and violent acts accounted for about 18 percent of fatal injuries in 2003 and are a major cause of fatalities among sales workers, police, and taxi and truck drivers.
- California agriculture has the fourth-highest incidence rate for fatal injuries. The major cause for fatalities in agriculture is motor vehicles, accounting for 47 percent of the total, while the major causes for non-fatal injuries in this industry are "struck by" and "overexertion," which together account for over 50 percent.⁵

Non-fatal and Fatal Occupational Injuries by Establishment Size and Type

- The lowest rate for total recordable non-fatal cases in 2002 was experienced by the smallest employers. Employers with 1 to 10 employees and 11 to 49 employees had incidence rates of 2.1 and 4.8 cases, respectively, per 100 full-time employees. Although small employers experienced the lowest incidence rates, they also experienced the biggest increase (20 percent) in their incidence rates since last year.
- Establishments with 50 to 249 and 250 to 999 employees reported the highest rate of 6.9 and 7.6 cases per 100 full-time employees.
- Establishments with 1,000 or more employees reported a rate of 6.7 per 100 full-time employees.
- Private-sector wage and salary workers accounted for 74 percent of fatal occupational injuries, followed by self-employed and government workers accounting for about 16 percent and 10 percent, respectively, of fatal injuries in 2003.

Types of Injuries

- Some types of work injuries have declined since 1996 in the private sector, while others have increased. The number of sprains and strains continued to decline from 1996, but these injuries remain by far the most common type of work injury accounting for about 39 percent of days-away-from-work cases in the private sector. Tendonitis, chemical burns, amputations, and multiple injuries have increased from 1996-2002 with the biggest increase, 39 percent, seen in amputations.

⁵ California Occupational and Environmental Health Division, UC Berkeley.

- Back injuries have decreased by about 12 percent since 1996 in the private sector, even though the back is the most frequently injured body part, accounting for almost 1 out of 4 days-away-from-work cases in the private sector and 1 out of 5 cases in local government.
- In the private sector, contact with objects and equipment was the leading cause of days-away-from-work injuries, cited in about 26 percent of days-away-from-work cases. Overexertion was the second common cause of injury, accounting for about 21 percent of injuries.
- In local government, the number one cause of injury was overexertion, accounting for 20 percent of local government's days-away-from-work cases in 2002.

Demographics

- Over the period from 1996 to 2002, the number of days-away-from-work cases for women decreased by about 4 percent. Days-away-from-work cases for men decreased by about 15 percent.
- Between 1996 and 2002, the youngest age groups (16 to 19, 20 to 24, 25 to 34, and 35 to 44) experienced a decline between 1996 and 2002 in non-fatal injuries. The biggest decline (49 percent) occurred among 16 to 19 year-old workers. All other age groups (45 to 54, 55 to 64, and 65 and over) experienced an increase in their days-away-from-work rates, with the biggest increase (74 percent) seen in the 65 years and over age group.
- In 2003, out of 456 fatalities, approximately 92 percent were male and 8 percent were female. Some age group categories – 18 to 19 years, 35 to 44 years, 65 years and over – experienced a decline in fatal injuries between 2002 and 2003, while others – 20 to 24 years and 25 to 34 years – experienced an increase. The biggest decline (48 percent) was seen in the 65 years and over age group and the biggest increase (36 percent) in the 20 to 24-year age group. The 55 to 64 age group did not experience an increase or a decline.
- The highest number of fatalities in 2003 by race or ethnic origin categories was experienced by “White, non-Hispanic” followed by “Hispanic or Latino,” accounting for 52 percent and 35 percent of the fatalities respectively. From 2002 to 2003, fatal injuries declined by 31 percent for the “Black, non-Hispanic” and by 9 percent for the “Hispanic or Latino”. Fatal injuries for the “White, non Hispanic” and “Asian” category remained the same since 2002.
- On the national level, the BLS reports that between 1995 and 2000, the Hispanic worker fatality rate was consistently above the overall national worker fatality rate. The reason for the higher incidence rates is that Hispanics are found working disproportionately in high-risk occupations. Occupations with the highest number of fatal injuries to Hispanics during 1995-2000 were construction laborers, truck drivers and farm workers.
- Between 1995 and 2000, California had the largest number of fatal work injuries, 1,112, to Hispanic native and foreign-born workers in the nation. Of these, 61 percent were injuries to Hispanic foreign-born workers.⁶

⁶ US Bureau of Labor Statistics, Census of Fatal Occupational Injuries

WORKERS' COMPENSATION SYSTEM PERFORMANCE

Introduction

The Commission on Health and Safety and Workers' Compensation (CHSWC) monitors the overall performance of the entire health and safety and workers' compensation system to determine whether it meets the State's Constitutional objective to "accomplish substantial justice in all cases expeditiously, inexpensively, and without encumbrance of any character."

In this section, CHSWC has attempted to provide performance measures to assist in evaluating the system impact on everyone, particularly workers and employers.

Through studies and comments from the community, CHSWC has compiled the following information pertaining to the performance of California's systems for health, safety and workers' compensation. Brief interpretations are provided with the graphical representations.

The first subsection deals with how well the system is operating in terms of the volume of workload and the timeliness of actions. These factors affect both employers and employees. The second subsection discusses the costs, which are of particular interest to employers. The impact on workers in terms of benefits and outcomes is the focus of the third subsection.

Administrative Operations

- Division of Workers' Compensation (DWC) Opening Documents
- Division of Workers' Compensation Hearings
- Division of Workers' Compensation Decisions
- Division of Workers' Compensation Lien Decisions
- Vocational Rehabilitation Plan Approvals and Disapprovals
- Vocational Rehabilitation Decisions and Orders After Conference
- Vocational Rehabilitation Plan Outcomes
- Division of Workers' Compensation Audits
- Disability Evaluation Unit
- Information and Assistance Unit
- Division of Worker' Compensation Staffing

Adjudication Simplification Efforts

- Division of Workers' Compensation Information System
- Carve-outs – Alternative Workers' Compensation Systems

Costs

- Workers' Compensation Premium
- Insured and Self-insured Employer Expenditures
 - Indemnity
 - Medical Benefits
- Average Cost per Claim by Type of Injury
- Private-sector Self-insured Employer Expenditures
- Vocational Rehabilitation Costs

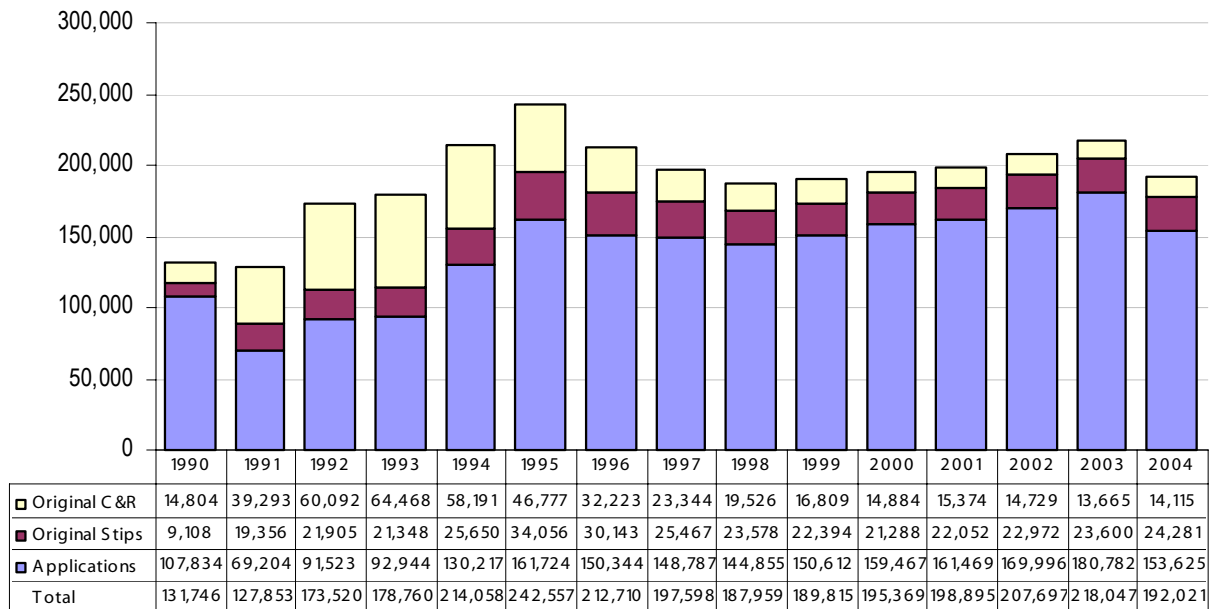
Administrative Operations

Division of Workers' Compensation Opening Documents

Three types of documents open a Workers' Compensation Appeals Board (WCAB) case. The chart below shows the numbers of Applications for Adjudication of Claim (Applications), Original Compromise and Releases (C&Rs), and Original Stipulations (Stips) received by the DWC.

The number of documents filed with the DWC to open a WCAB case on a workers' compensation claim has fluctuated during the early- and mid-1990's, leveled off during the late 1990's, increased slightly between 2000 and 2003, and decreased between 2003 and 2004.

DWC Opening Documents



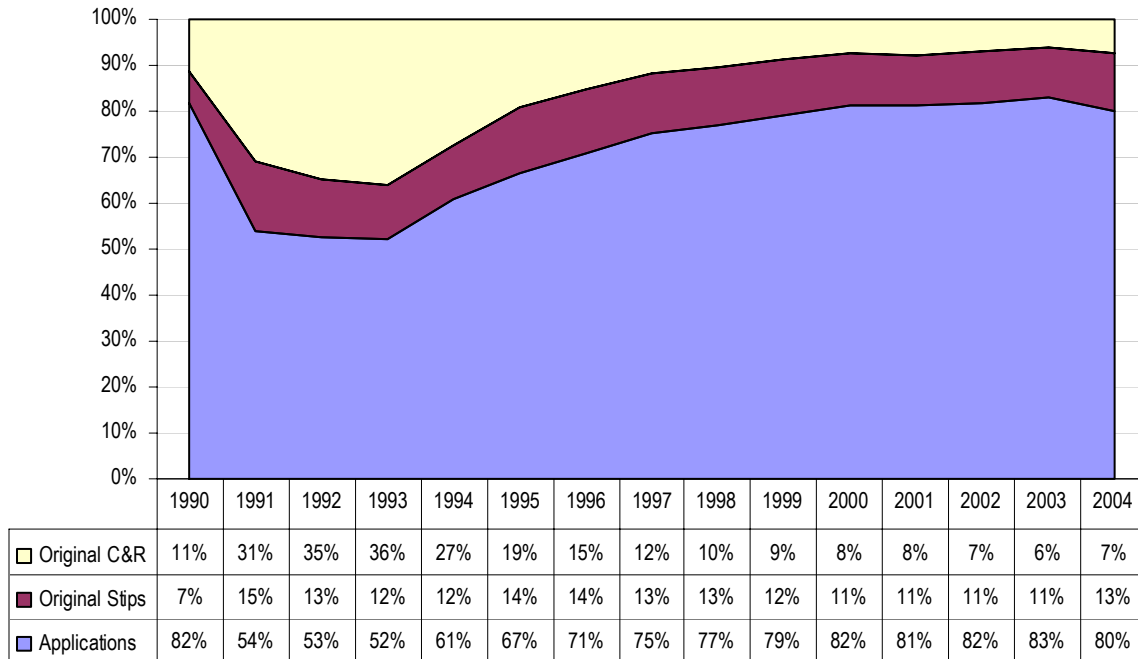
Source: DWC

The period from 1991 to 1992 shows growth in all categories of case-opening documents, followed by a year of leveling off between 1992 and 1993. The period from 1993 to 1995 is one of substantial increases in Applications, slight increases in Stips and significant decreases in C&Rs. Through 2003, Stips and C&Rs continued to decline, while Applications have increased slightly. In 1994, the situation was reversed with Application declining, and C&Rs and Stips increased slightly.

Mix of Opening Documents

As shown in the graph below, the proportion or “mix” of the types of case-opening documents received by the DWC varied during the 1990’s.

Percentage by Type of Opening Documents



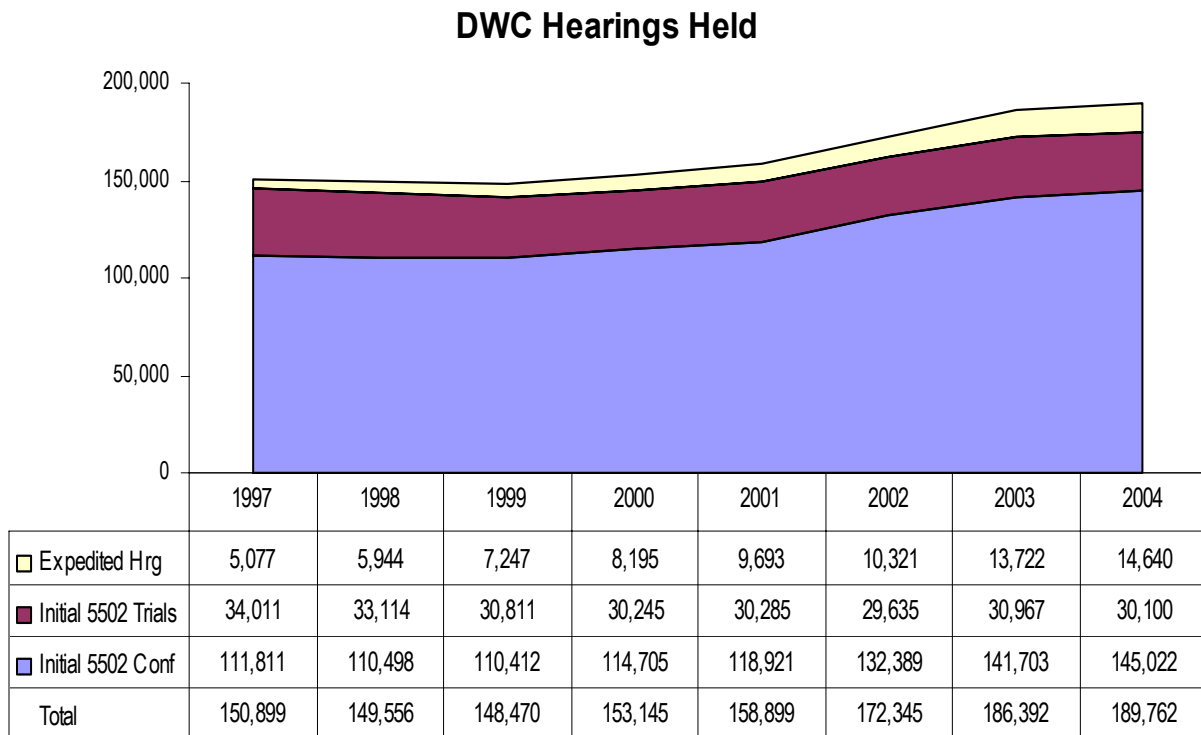
Source: DWC

Applications initially dropped from about 80 percent of the total in 1990 to less than 60 percent in 1991, reflecting increases in both original Stips and C&Rs. The numbers of Applications were steady from 1991 to 1993, and then rose again through 2003. The proportion of original (case-opening) Stips and original C&Rs declined slightly from 1999 to 2003.

Division of Workers' Compensation Hearings

Numbers of Hearings

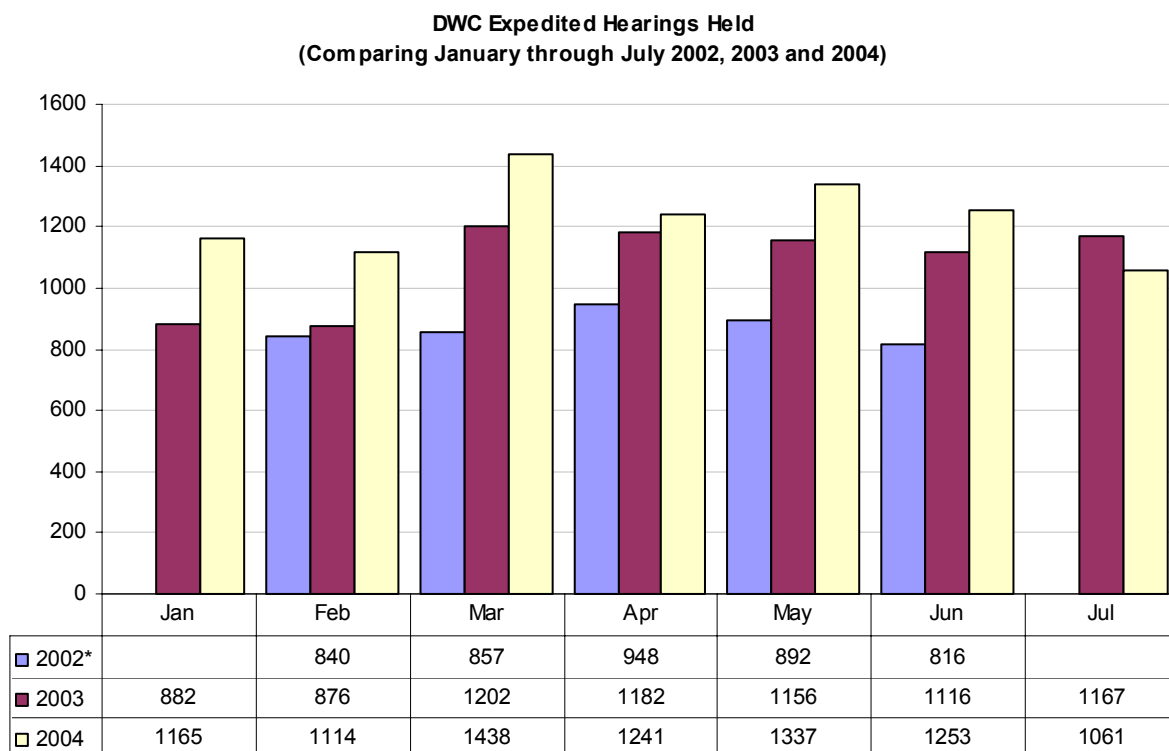
The chart below indicates the numbers of different types of hearings held in DWC from 1997 through 2004. Expedited hearings for certain cases, such as determination of medical necessity, may be requested pursuant to Labor Code Section 5502(b). Per Labor Code Section 5502(d), Initial 5502 Conferences are to be conducted in all other cases within 30 days of the receipt of a Declaration of Readiness (DR), and Initial 5502 Trials are to be held within 75 days of the receipt of a DR if the issues were not settled at the Initial 5502 Conference.



Source: DWC

DWC Expedited Hearings – First Seven Months of 2002-2004

This chart compares the number of expedited hearings from January through July of 2002, 2003, and 2004. Except for July, the numbers of hearings during each month increased from year to year.



*Please note that data was not available for Jan and Jul 2002.

Data Source: DWC

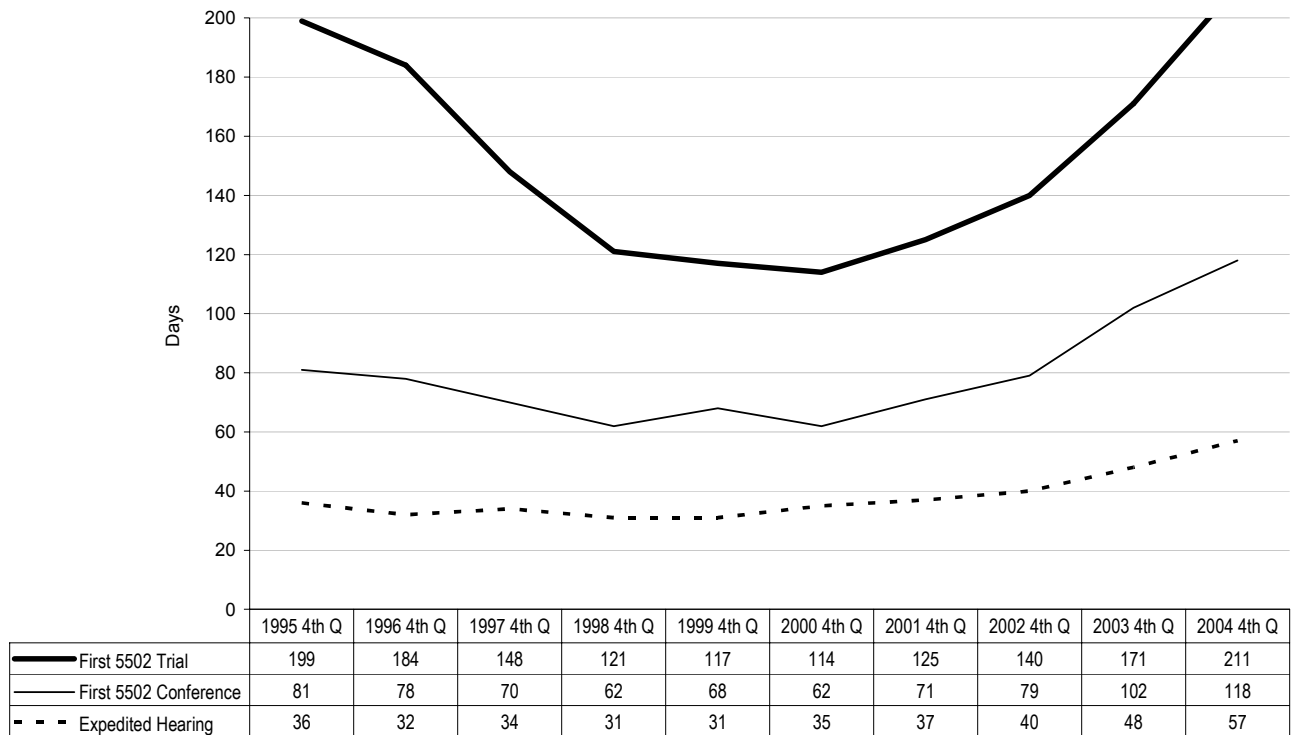
Timeliness of Hearings

California Labor Code Section 5502 specifies the time limits for various types of hearings conducted by the DWC on WCAB cases.

In general:

- A conference is required to be held within 30 days of the receipt of a request in the form of a DR.
- A trial must be held either within 60 days of the request or within 75 days if a settlement conference has not resolved the dispute.
- An expedited hearing must be held within 30 days of the receipt of the DR.

Elapsed Time in Days from Request to DWC Hearing



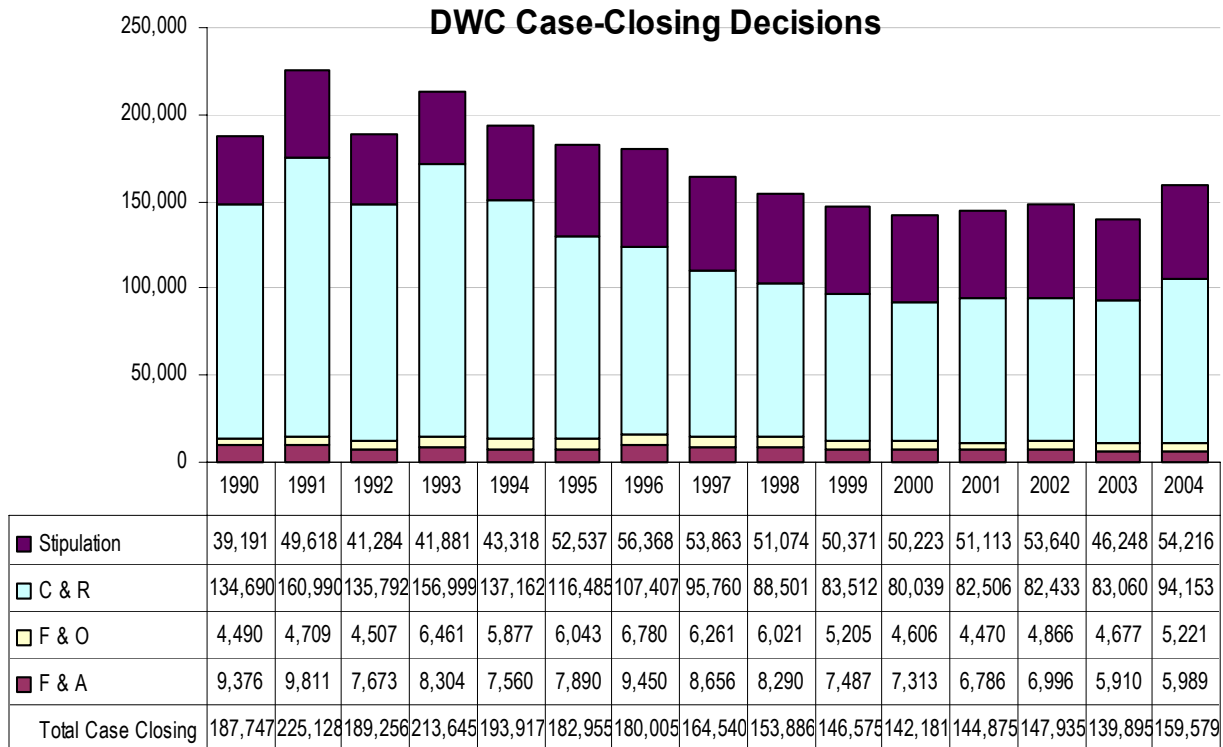
Source: DWC

As the above chart shows, the average elapsed time from a request to a DWC hearing decreased in the mid- to late-1990's and then remained fairly constant thereafter. Nevertheless, as of 2003, all of the average elapsed times have increased from the previous year's quarter, and none are within the statutory requirements.

Division of Workers' Compensation Decisions

Division of Workers' Compensation Case-closing Decisions

The following data indicate that the number of decisions made by the DWC that are considered to be case-closing have declined overall during the 1990's, with a slight increase from 2000 to 2002, followed by a decrease in 2003.



Source: DWC

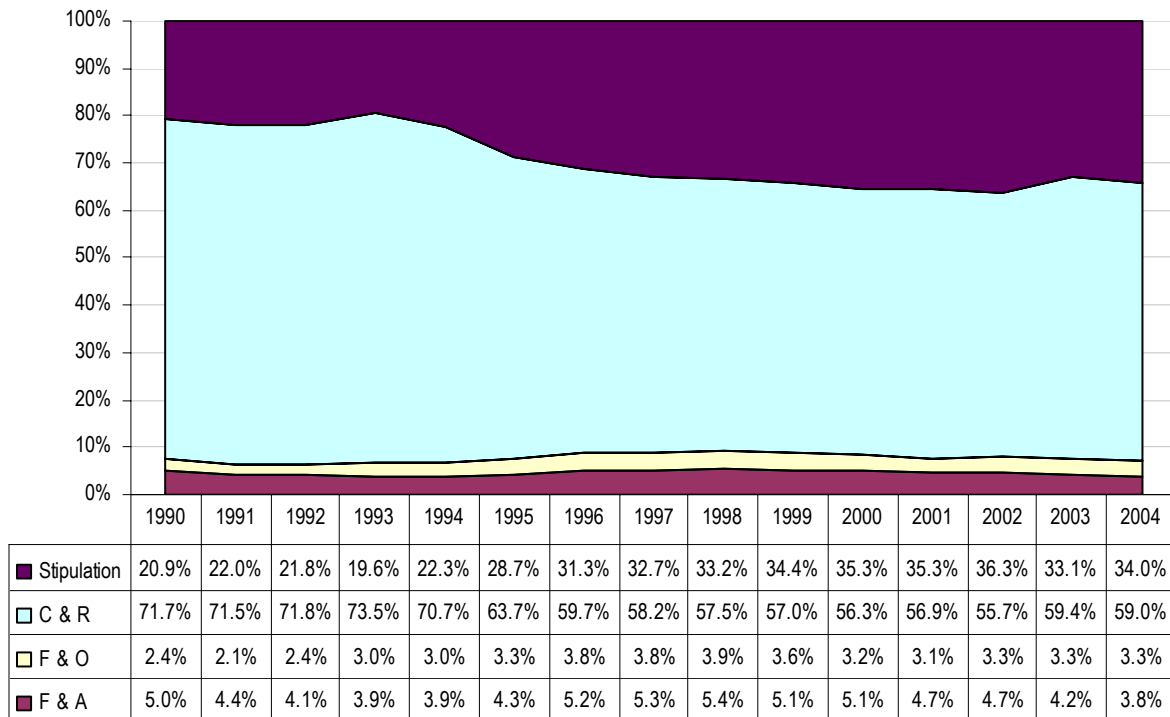
- The numbers of Findings and Awards (F&As) have shown an overall decline of 36.5 percent from 1990 to 2003.
- Findings and Orders (F&Os) increased during the first part of the decade and then declined to the original level in 2002, decreasing slightly from 2002 to 2003.
- Stips were issued consistently throughout the decade. The numbers of Stips issued rose from 1990 to 1991, declined from 1991 to 1992, leveled off from 1992 to 1994, rose again in 1995 and 1996, remained stable through 2000, increased slightly in 2001 and 2002, and decreased in 2003.
- The use of C&Rs decreased by half during the 1990's and into the millennium. C&Rs declined steadily from 1993 through 2000, increased in 2001, and remained stable in 2002 and 2003.

Mix of Division of Workers' Compensation Decisions

As shown on the charts on the previous page and this page the vast majority of the case-closing decisions rendered during the 1990's were in the form of a WCAB judge's approval of Stips and C&Rs which were originally formulated by the case parties.

Only a small percentage of case-closing decisions evolve from an F&A or F&O issued by a WCAB judge after a hearing.

DWC Decisions
Percentage distribution by type of decision



Source: DWC

During the period from 1993 through the beginning of 2000 and beyond, the proportion of Stips rose, while the proportion of C&Rs declined. This reflects the large decrease in the issuance of C&Rs through the 1990's.

Division of Workers' Compensation Lien Decisions

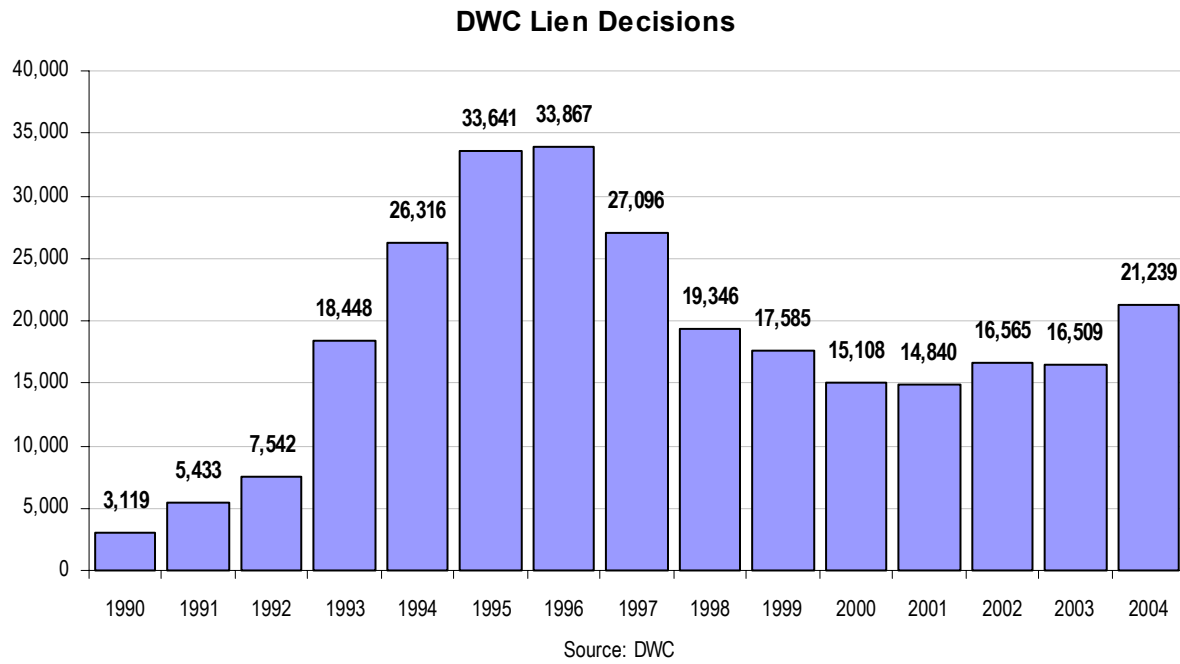
The DWC has been dealing with a large backlog of liens filed on WCAB cases. Many of the liens have been for medical treatment and medical-legal reports.

However, liens are also filed to obtain reimbursement for other expenses:

- The Employment Development Department (EDD) files liens to recover disability insurance indemnity and unemployment benefits paid to industrially injured workers.
- Attorneys have an implied lien during representation of an injured worker. If an attorney is substituted out of a case and seeks a fee, the attorney has to file a lien.
- District Attorneys file liens to recover spousal and/or child support ordered in marital dissolution proceedings.
- Occasionally, a landlord or grocer will claim a lien for living expenses of the injured or his/her dependents.
- Although it is relatively rare now, occasionally, a private disability insurance policy will file a lien on workers' compensation benefits on the theory that the proceeds from the benefits were used for living expenses of the injured worker.
- Some defendants will file liens in lieu of petitions for contribution where they have paid or are paying medical treatment costs to which another carrier's injury allegedly contributed.
- Liens are sometimes used to document recoverable (non-medical) costs, e.g., photocopying of medical records, interpreters' services and travel expenses.

These data indicate a large growth in decisions regarding liens filed on WCAB cases and a concomitant expenditure of DWC staff resources on the resolution of those liens.

Labor Code Section 4903.05, added by Senate Bill (SB) 228, requires that a filing fee of \$100 be charged for each initial lien filed by a medical provider, excluding the Veterans Administration, the Medi-Cal program, or public hospitals. SB 899 amended Section 4903.05 to provide that persons filing liens on behalf of medical providers may also pay the \$100 filing fee.

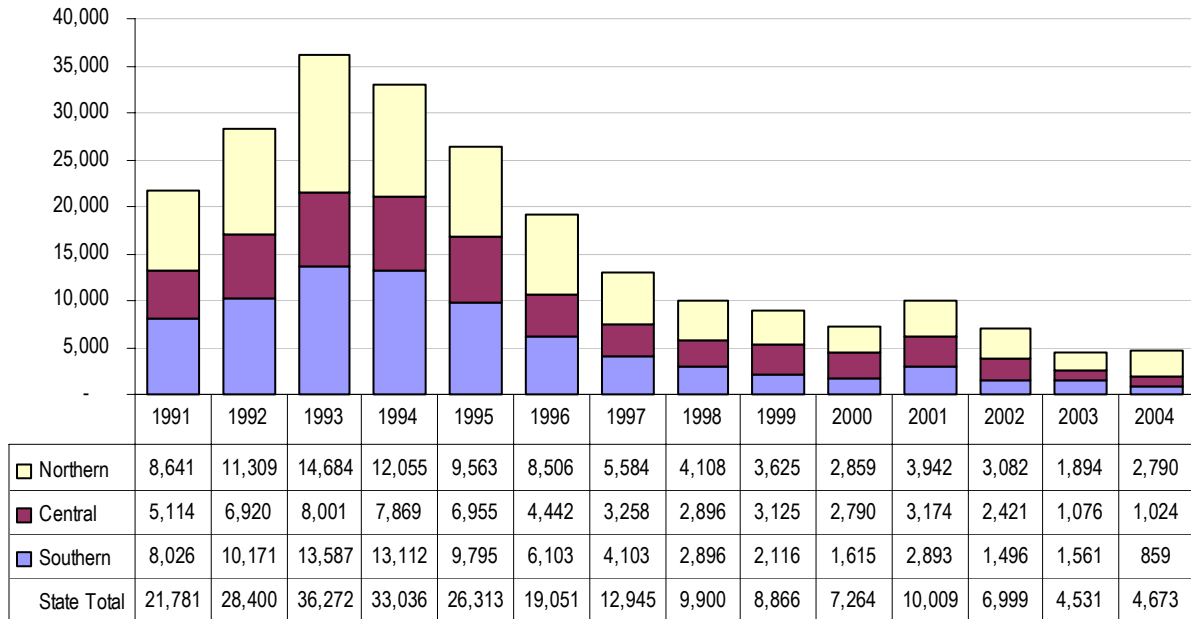


Vocational Rehabilitation Decisions

Vocational Rehabilitation Plan Approvals and Disapprovals

The number of vocational rehabilitation plans approved by the DWC has declined steadily from 1993 to 2000, increased in 2001, declined again in 2002, and remained fairly constant from 2002 to 2003.

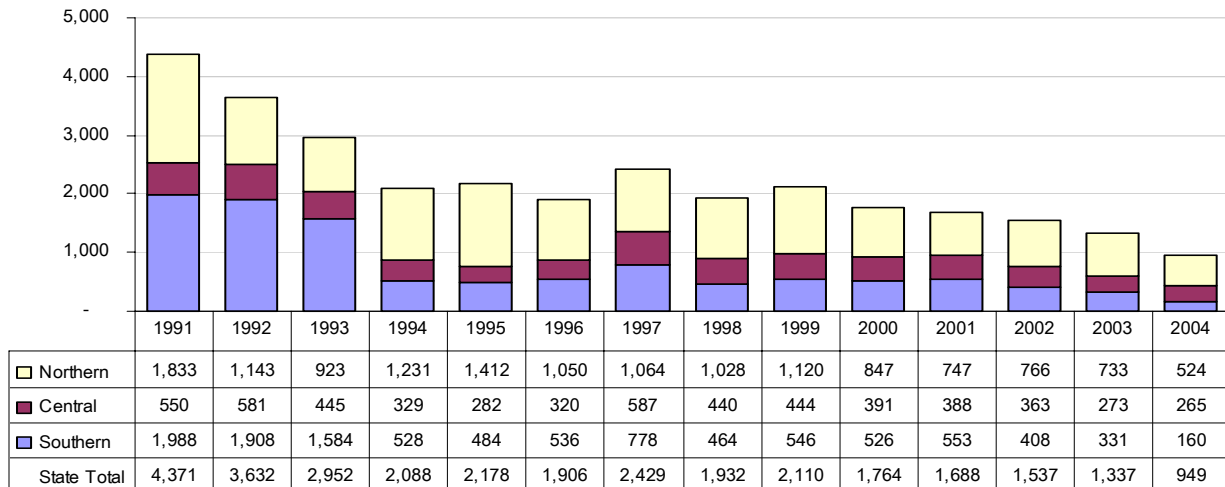
DWC Vocational Rehabilitation Plan Approvals



Source: DWC

Vocational Rehabilitation Plan Disapprovals

Vocational Rehabilitation Plan Disapprovals by DWC Region



Source: DWC

Vocational Rehabilitation Decisions and Orders After Conference

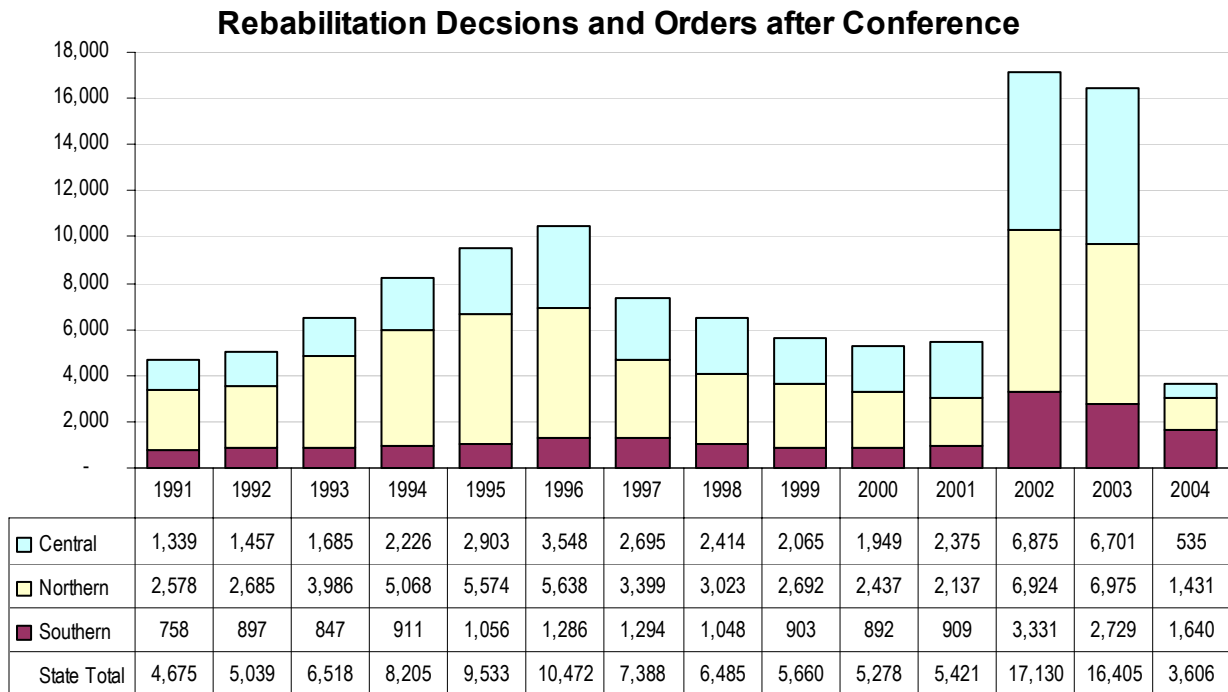
Vocational rehabilitation decisions declined from 1996 to 2000, increasing slightly in 2001.

There were 8,930 more cases referred to the DWC Vocational Rehabilitation Unit in 2002 than in 2001, an increase of approximately 28 percent. The increase in cases is directly reflected in the increase in disputes received by the Unit in 2002. There were actually 10,562 more disputes filed in 2002 than in 2001.

In 2001, the Unit held 5,421 conferences, whereas in 2002, 17,130 conferences were held, an increase of more than 200 percent. It should be noted that this is the first year where the Unit held more conferences to issue determinations on the record (17,130 as compared to 16,973).

The Rehabilitation Unit held 16,405 conferences as a result of disputes filed in 2003, a slight decrease from the previous year.

Vocational Rehabilitation Decisions and Orders After Conference



Source: DWC

Fraud

Suspected Fraudulent Claims

| Fiscal Year | Suspected Fraudulent Claims |
|-------------|-----------------------------|
| 1992-93 | 8,342 |
| 1993-94 | 7,284 |
| 1994-95 | 4,004 |
| 1995-96 | 3,947 |
| 1996-97 | 3,281 |
| 1997-98 | 4,331 |
| 1998-99 | 3,363 |
| 1999-00 | 3,362 |
| 2000-01 | 3,548 |
| 2001-02 | 2,968 |
| 2002-03 | 3,544 |

Source: California Department of Insurance, Fraud Division

According to the CDI Fraud Division, the number of suspected fraudulent claims has fluctuated around 3,500 annually. Several reasons for this trend include:

- Lower claims frequency.
- Removal of major medical and legal mills involved in illegal activities.
- Reduction in insurers' special investigation units (SIUs).
- Fewer insurance companies in the California workers' compensation market.
- Deterrence effect resulting from statewide anti-fraud efforts of local district attorneys, the Fraud Division and the insurance industry.

After a fraud referral, an investigation must take place before any arrests are made. The average time from referral to arrest is usually around nine months. For this reason, the number of arrests does not necessarily correspond to the number of referrals in a particular year.

Workers' Compensation Fraud Suspect Arrests

| Fiscal Year | Fraud Suspect Arrests |
|-------------|-----------------------|
| 1992-93 | 24 |
| 1993-94 | 116 |
| 1994-95 | 163 |
| 1995-96 | 202 |
| 1996-97 | 207 |
| 1997-98 | 298 |
| 1998-99 | 216 |
| 1999-00 | 226 |
| 2000-01 | 170 |
| 2001-02 | 290 |
| 2002-03 | 369 |

Source: California Department of Insurance, Fraud Division

Workers' Compensation Fraud Suspect Convictions

| Fiscal Year | Fraud Suspect Convictions |
|--------------------|---------------------------|
| 1993-94 | 181 |
| 1994-95 | 198 |
| 1995-96 | 248 |
| 1996 calendar year | 177 (CWCI) |
| 1997 calendar year | 299 (CWCI) |
| 1998 calendar year | 268 (CWC) |
| 1999 calendar year | 258 (CWCI) |
| 2000-01 | 367 |
| 2001-02 | 263 |
| 2002-03 | 293 |

Source: California Department of Insurance, Fraud Division and California Workers' Compensation Institute

Types of Workers' Compensation Fraud Investigations

The following table indicates the number and types of investigations opened and carried for fiscal years 2001-02 and 2002-03. Applicant fraud appears to be the area generating the most cases followed by premium fraud and medical provider fraud.

| Type of Investigation | Fiscal Year 2002-03 Cases Number/Percent | Fiscal Year 2001-02 Cases Number/Percent |
|-----------------------|---|---|
| Applicant | 1,263 - 72.63% | 1,293 - 79.37% |
| Premium | 207 - 11.90% | 159 - 9.76% |
| Fraud Rings | 7 - 0.4% | 1 - 0.06% |
| Capping | 5 - 0.28% | 6 - 0.37% |
| Medical Provider | 97 - 5.6% | 98 - 6% |
| Insider | 6 - 0.34% | 8 - .49% |
| Other | 93 - 5.3% | 64 - 3.93% |
| Uninsured | 61 - 3.5% | N/A |
| TOTAL | 1,739 | 1,629 |

Source: California Department of Insurance, Fraud Division

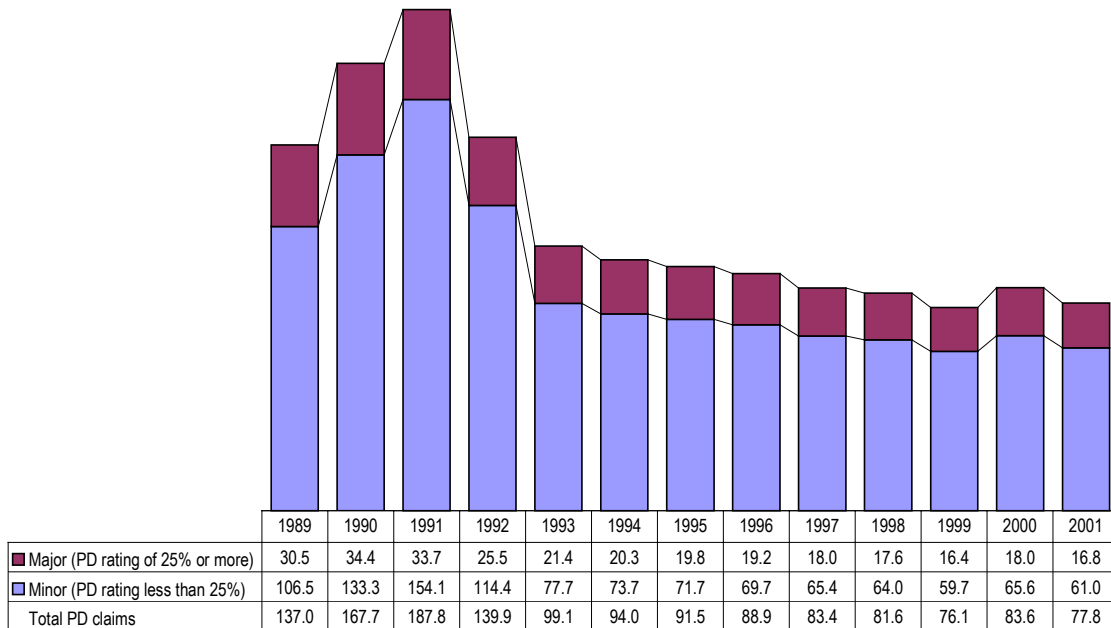
Geographically, the great majority of suspected fraud cases come from Los Angeles County (21 percent) followed by Sonoma and San Bernardino Counties at 7 percent of cases.

Permanent Disability and Medical/Legal Expenses

Permanent Disability Claims

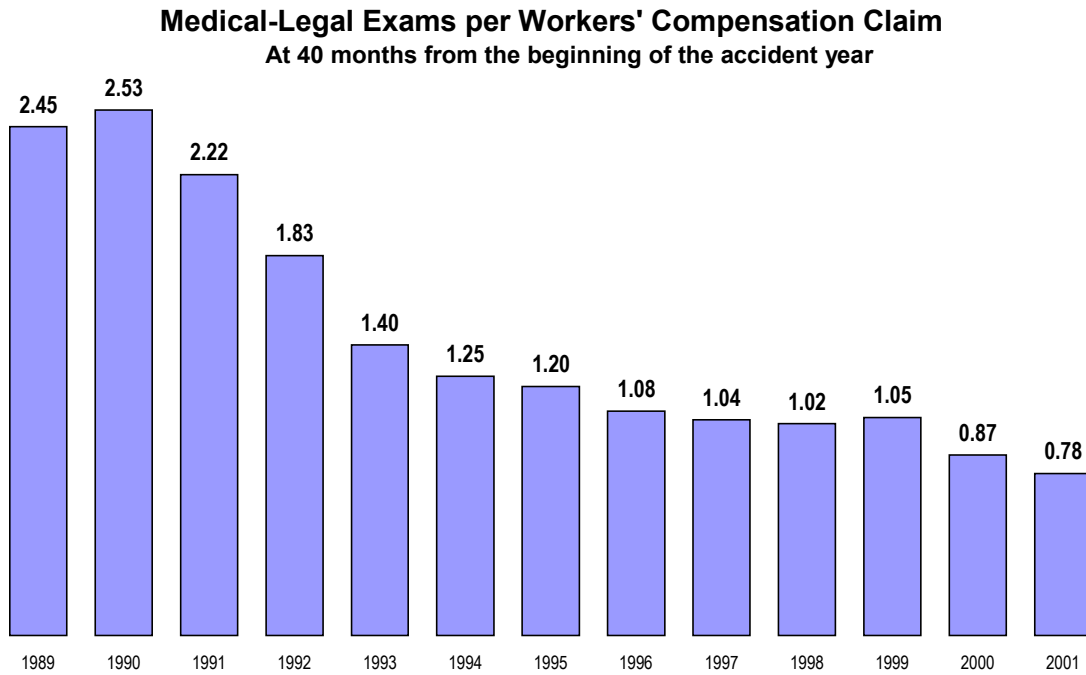
The following chart displays the number of permanent partial disability (PPD) claims during each calendar year since 1989. Up through 1993, the Workers' Compensation Insurance Rating Bureau (WCIRB) created these data series from Individual Case Report Records submitted as part of the Unit Statistical Report. Since that time, the series has been discontinued, and estimates for 1994 and subsequent years are based on policy-year data adjusted to the calendar year and information on the frequency of all claims, including medical-only claims, that are still available on a calendar-year basis.

PPD Claims at Insured Employers
(In thousands, by year of injury)



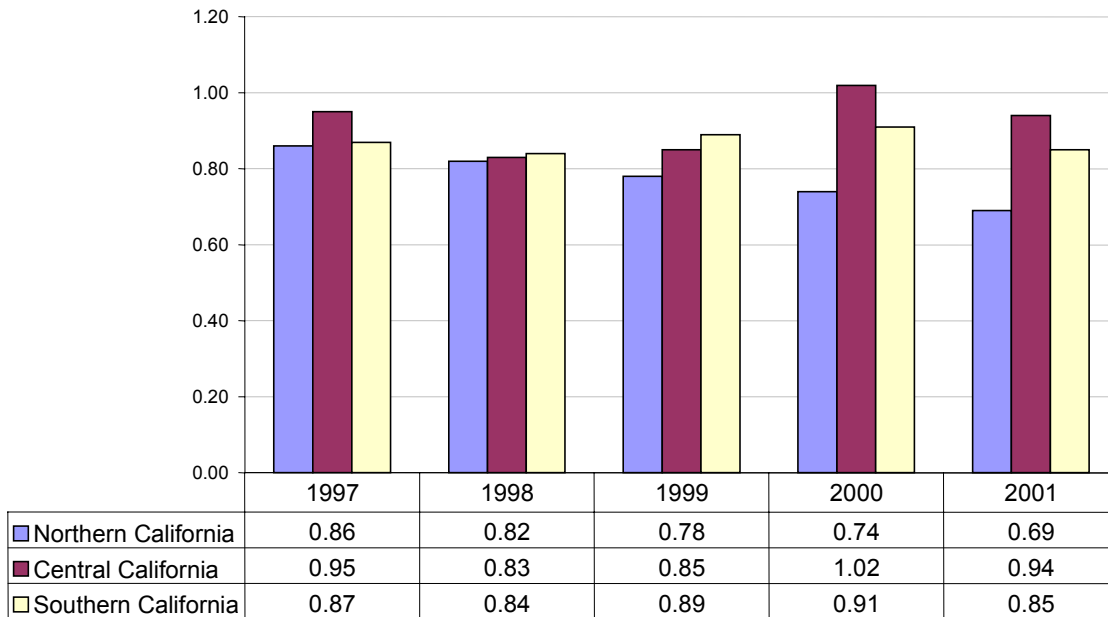
Source: WCIRB PD Survey

Medical-legal Examinations per Claim



Source: WCIRB PD Survey

Average Number of Medical-Legal Exams per Claim by Region (at 34 months after beginning of accident year)

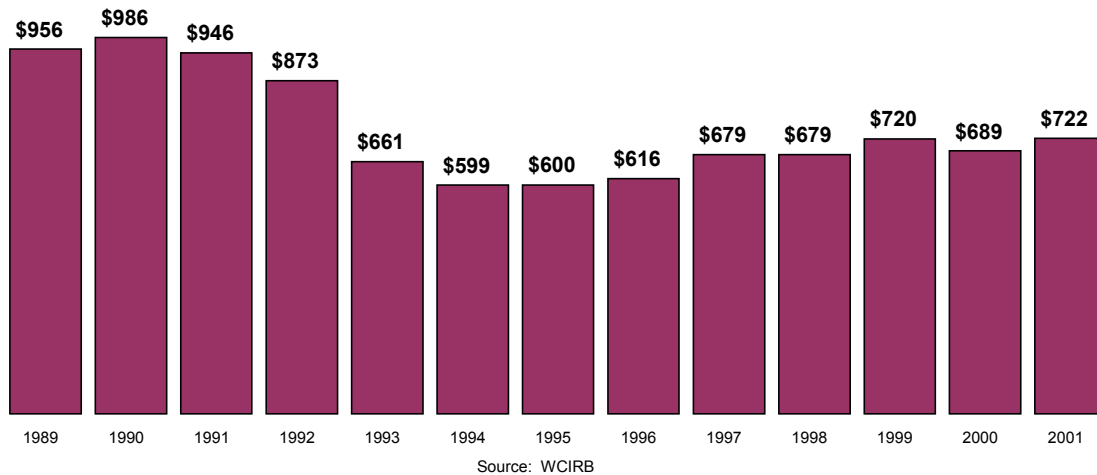


Source: WCIRB

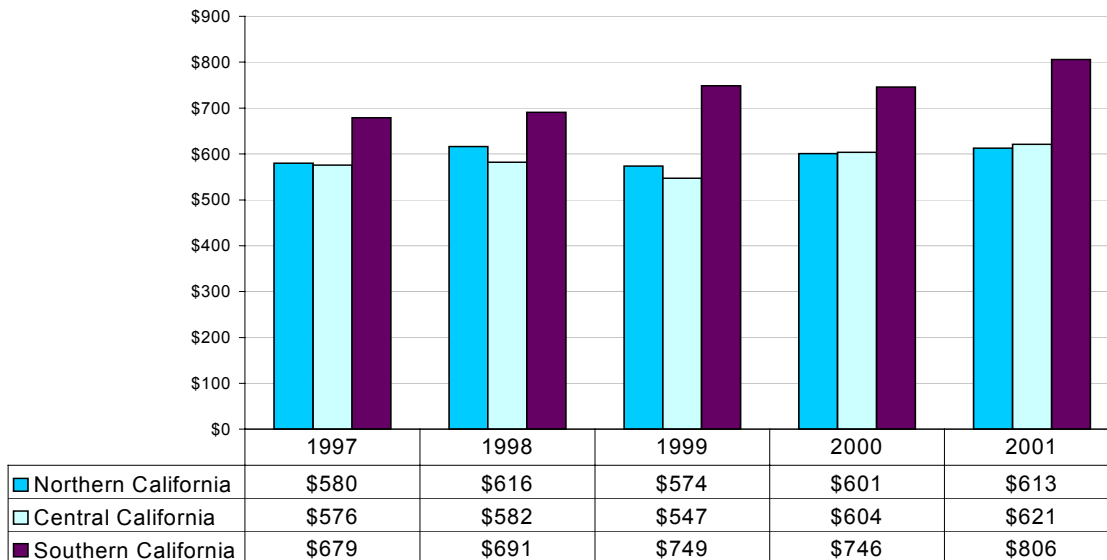
Cost per Medical-legal Examination

There are two reasons why the average cost per medical examination has declined by 27 percent since its peak in 1990. Second, during this period, the average cost of medical examinations was also being affected by the frequency of psychiatric examinations. On average, psychiatric examinations are the most expensive examinations by specialty of provider. The relative portion of all examinations that is psychiatric examinations has declined since hitting a high in 1990-91, leading to a substantial improvement in the overall average cost per examination.

Average Cost of Medical-Legal Exam
(Evaluated at 40 months after beginning of accident year)



Average Cost of Medical-Legal Exam by Region
(at 34 months after beginning of accident year)



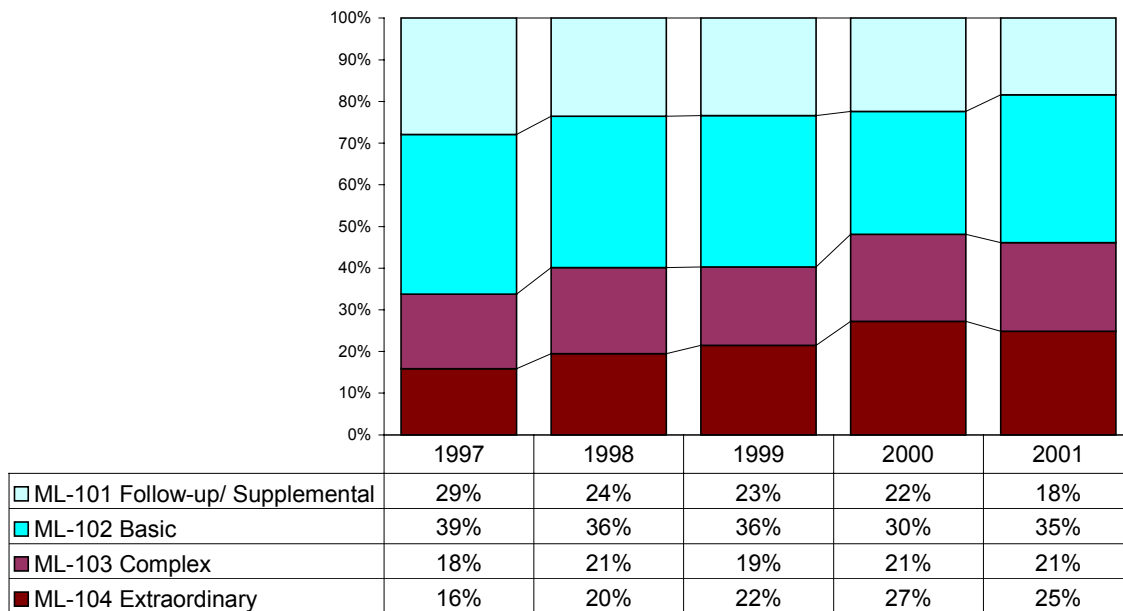
The survey data show that, on average, reports done in southern California have always been substantially more expensive. Increases in the average cost are being driven by claims in Southern California.

Further analysis indicates that the cost driver for the southern California trend is not the price paid for specific types of examinations. Rather, the mix of codes under which the reports are billed has changed to include a higher percentage of the most complex and expensive examinations and fewer of the least expensive type. The following table shows the cost and description from the Medical-Legal Fee Schedule.

| Evaluation Type | Amount Presumed Reasonable |
|-----------------------------------|----------------------------|
| ML-101 Follow-up/ Supplemental | \$250 |
| ML-102 Basic | \$500 |
| ML-103 Complex | \$750 |
| ML-104 Extraordinary | \$200/hour |

The following chart indicates that the distribution of examinations in southern California has shifted away from ML-101 examinations to include a higher percentage of ML-104 examinations with "Extraordinary" complexity. At the same time, the average cost within each examination type did not exhibit a trend.

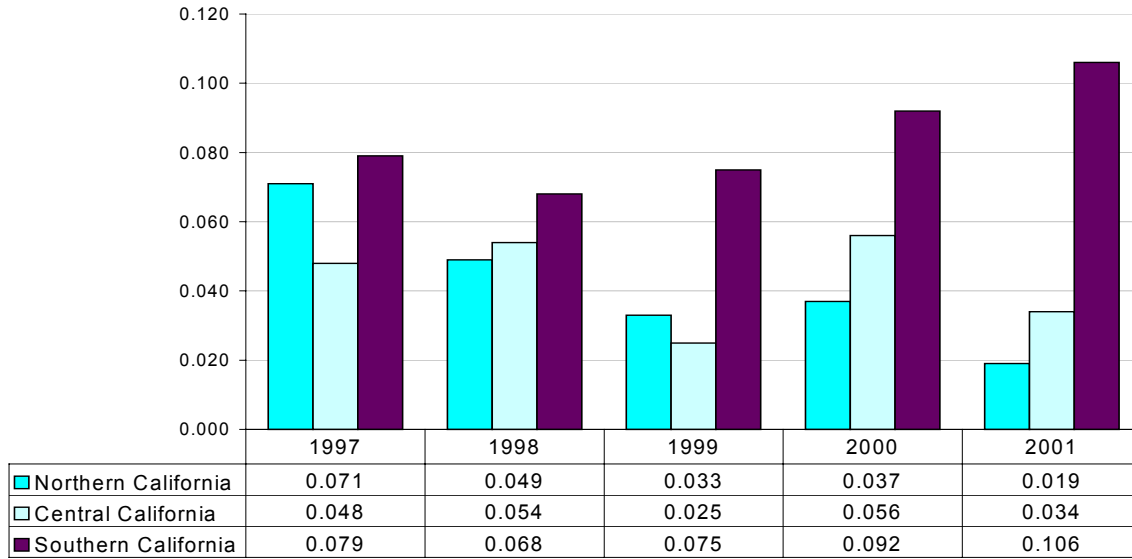
**Distribution of Medical-Legal Exam by Type
(Southern California)**



Source: WCIRB

Another possible explanation for the differing trends in the average cost per report and the increasing frequency of the most complex examinations in southern California is that psychiatric evaluations are more common in southern California. In addition, while the percent of PPD claims with psychiatric evaluations declined in the other two regions between 1997 and 2000, this was not true in the south. Psychiatric examinations are nearly always billed under the ML-104 code that is the most expensive.

**Average Number of Psychiatric Exams
per PPD Claim by Region**



Medical-legal Cost Calculation

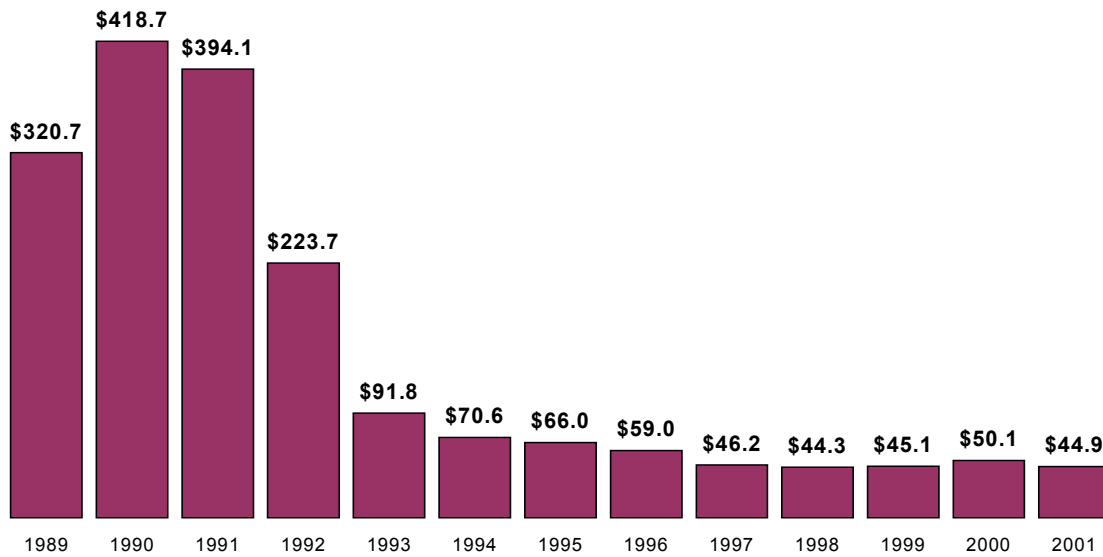
Total medical-legal costs are calculated by multiplying the number of PPD claims by the average number of medical-legal examinations per claim and by the average cost per medical-legal examination.

$$\text{Total Medical-Legal Cost} = \text{Number of PPD Claims} * \text{Average Number of Exams/Claim} * \text{Average Cost/Exam}$$

Medical-legal Costs

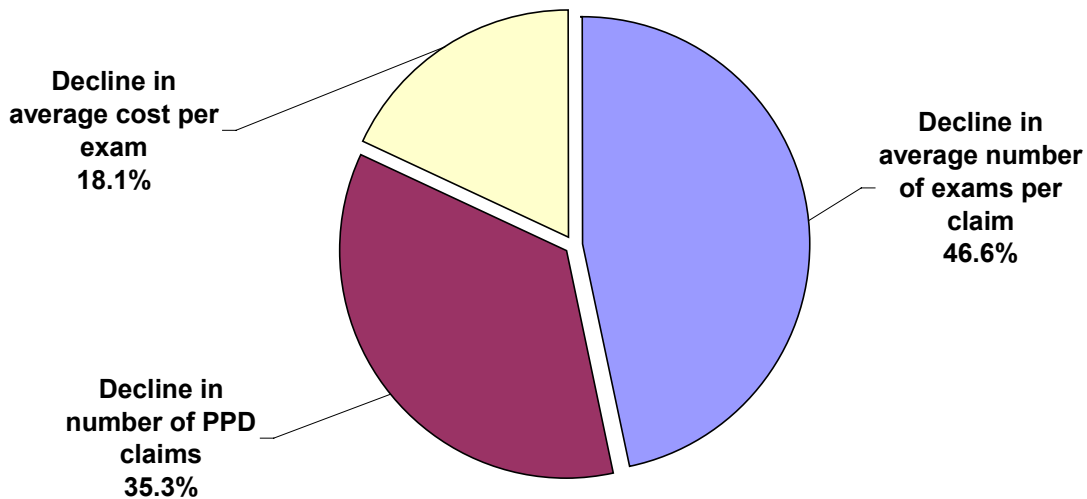
During the 1990's, the cost of medical-legal examinations improved dramatically. For the insured community, the total cost of medical-legal examinations performed on PPD claims by 40 months after the beginning of the accident year has declined from a high of \$419 million in 1990 to an estimated \$44.9 million for injuries occurring in 2001. This is an 89 percent decline since the beginning of the decade.

Medical-Legal Costs on PPD Claims at Insured Employers
(In Million\$, 40 months after beginning of accident year)



Source: WCIRB PD Survey

Sources of Savings
Medical-Legal Costs on PPD Claims 1990-2001



Source: WCIRB

CARVE-OUTS - ALTERNATIVE WORKERS' COMPENSATION SYSTEMS

A provision of the workers' compensation reform legislation in 1993, implemented through Labor Code Section 3201.5, allowed construction contractors and unions, via the collective bargaining process, to establish alternative workers' compensation programs, also known as carve-outs.

CHSWC is monitoring the carve-out program, which is administered by the DWC.

As shown in the following table, participation in the carve-out program has grown, with significant increases in the number of employees, work hours and amount of payroll.

| Carve Out Participation | 1995 | 1996 | 1997 | 1998 | 1999 | 2000* | 2001* | 2002 |
|----------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Employers | 242 | 277 | 550 | 683 | 442 | 260 | 143 | 512 |
| Work Hours (millions) | 6.9 million | 11.6 million | 10.4 million | 18.5 million | 24.8 million | 16.9 million | 7.9 million | 29.4 million |
| Employees (full-time equivalent) | 3,450 | 5,822 | 5,186 | 9,250 | 12,395 | 8,448 | 3,949 | 14,261 |
| Payroll (millions \$) | \$157.6 million | \$272.4 million | \$242.6 million | \$414.5 million | \$585.1 million | \$442.6 million | \$201.9 million | \$634.2 million |

* Please note that data is incomplete

Source: DWC

A listing of employers and unions in carve-out agreements follows.

CHSWC engaged in a study to identify the various methods of alternative dispute resolution that are being employed in California carve-outs and to begin the process of assessing their efficiency, effectiveness and compliance with legal requirements.

Since carve-out programs have operated only since the mid-1990's, the data collected are very preliminary and not statistically significant. The study team found indications that neither the most optimistic predictions about the effects of carve-outs on increased safety, lower dispute rates, far lower dispute costs, and significantly more rapid return to work, nor the most pessimistic predictions about the effect of carve-outs on reduced benefits and access to representation have occurred.

Carve-out Participants as of December 20, 2004

The following charts show the current status of carve-out agreements pursuant to Labor Code Sections 3201.5 and 3201.7, as reported by the DWC.

Non-construction Industry Carve-out Participants as of December 20, 2004 Labor Code Section 3201.7

| No | Union | Company | Permission to neg. date/expires | App'n for Agrmt Acptnce | Agrment Acceptn Ltr date |
|----|--|--|---------------------------------|-------------------------|--------------------------|
| 1. | United Food & Commercial Workers Union Local 324 | Super A Foods- 2 locations 76 employees | 09/01/04- 09/01/05 | | |
| 2. | United Food & Commercial Workers Union Local 1167 | Super A Foods - Meat Department 8 employees | 09/01/04- 09/01/05 | | |
| 3. | Teamsters Cal. State Council- Cannery & Food Processing Unions, IBT, AFL-CIO | Cal. Processors, Inc. Multi-Employer Bargaining Representative | 7-06-04/ 7-05-05 | | |
| 4. | United Food & Commercial Workers Union Local 770 | Super A Foods - 10 locations - ~ 283 members | 09/01/04- 09/01/05 | | |
| 5. | United Food & Commercial Workers Union Local 1036 | Super A Foods - All employees, except those engaged in janitorial work or covered under a CBA w/Culinary Workers and demonstrators | 09/01/04- 09/01/05 | | |
| 6. | Operating Engineers-Loc 3 Non- Construction | Basic Crafts Workers' Compensation Benefits Trust Fund | 12/09/04- 12/09/05 | | |
| 7. | Laborers - Non-Construction | Basic Crafts Workers' Compensation Benefits Trust Fund | 12/09/04- 12/09/05 | | |
| 8. | Carpenters- Non-Construction | Basic Crafts Workers' Compensation Benefits Trust Fund | 12/09/04- 12/09/05 | | |

Source: DWC

**Construction Carveout Participants as of December 20, 2004.
Labor Code Section 3201.5**

(1) = 1 employer, 1 union; (2) = 1 union, multi employer; (3) = project labor agreement

| No. | Union | Company | Exp. Date |
|---------|--|--|-----------|
| 1. (3) | CA Building and Construction Trades Council | Metropolitan Water District of Southern CA | 10/7/06 |
| 2. (2) | International Brotherhood of Electrical Workers - IBEW | NECA--National Electrical Contractors Association. | 8/14/07 |
| 3. (2) | Southern CA District Council of Carpenters and 19 local unions | Six multi-employer groups - 1000 contractors. | 8/14/07 |
| 4. (2) | Southern CA Pipe Trades Council 16 | Multi employer group - Plumbing and Piping Industry Council | 8/24/07 |
| 5. (1) | Steamfitters Local 250 | Cherne - two projects completed in 1996 | Completed |
| 6. (1) | International Union of Petroleum and Industrial Workers | TIMEC Co., Inc./TIMEC Southern CA, Inc. | 7/31/04 |
| 7. (3) | Contra Costa Building and Construction Trades Council | Contra Costa Water District - three project labor agreements Los Vaqueros | Completed |
| 8. (2) | Southern CA District Council of Laborers | Associated General Contractors of CA, Building Industry Association. of Southern CA, Southern CA Contractors' Association., Engineering Contractors' Association | 7/31/02 |
| 9. (3) | CA Building and Construction Trades Council | Metropolitan Water District Of Southern CA Inland Feeder - Parsons | Completed |
| 10. (3) | Building and Construction Trades Council of Alameda County | Parsons Constructors, Inc. - National Ignition Facility - Lawrence Livermore | 9/23/06 |
| 11. (2) | District Council of Painters No. 36 | Los Angeles County Painting and Decorating Contractors Association. | 10/29/06 |
| 12. (1) | Plumbing and Pipefitting Local 342 | Cherne Contracting - Chevron Base Oil 2000 project | Completed |
| 13. (3) | Los Angeles County Building and Construction Trades Council | Cherne-ARCO | Completed |
| 14. (2) | Operating Engineers Local 12 | Southern CA Contractors' Association. | 4/1/05 |
| 15. (2) | Sheet Metal International Union | Sheet Metal and A/C Contractors National Association. (SMACNA) | 4/1/05 |
| 16. (3) | Building and Construction Trades Council of San Diego | San Diego County Water Authority Emergency Storage Project | 2/20/06 |

Selected Indicators in Workers' Compensation: A Report Card for Californians

| No. | Union | Company | Exp. Date |
|---------|--|---|-----------|
| 17. (3) | Los Angeles County Building and Construction Trades Council | Cherne Contracting - Equilon Refinery - Wilmington | 3/1/04 |
| 18. (3) | Plumbing and Pipefitting Local 342 | Cherne Contracting - Chevron Refinery - Richmond | 7/1/05 |
| 19. (3) | Plumbing and Pipefitting Local 342 | Cherne Contracting - Tosco Refinery - Martinez | 7/1/05 |
| 20. (3) | Los Angeles/Orange Counties Construction Trade Council | Cherne Contracting - Chevron Refinery - El Segundo | 7/26/05 |
| 21. (2) | District Council of Iron Workers of the State of California and Vicinity | California Ironworker Employees Council | 2/25/06 |
| 22. (2) | Sheet Metal Workers International Assn. #105 | Sheet Metal and A/C Labor Management Safety Oversight Committee (LMSOC) | 4/17/06 |
| 23. (2) | United Union of Roofers, Waterproofers and Allied Workers, Locals 36 and 220 | Southern California Union Roofing Contractors Assn. | 4/7/06 |
| 24. (2) | United Union of Roofers, Waterproofers and Allied Workers, Locals 40, 81, and 95 | Associated Roofing Contractors of the Bay Area Counties | 7/31/05 |
| 25. (2) | United Association of Journeyman & Apprentices-- Plumbers & Pipefitters, Local 447 | Northern CA Mechanical Contractors Assoc. (NCMCA & Associated Plumbing & Mechanical Contractors of Sacramento, Inc. (APMC) LMSOC) | 11/7/06 |
| 26. (2) | Operatives Plasterers and Cement Masons International Association, Local 500 & 600 | So. California Contractors Association, Inc | 4/1/05 |
| 27. (1) | International Unions of Public & Industrial Workers | Irwin Industries, Inc | 3/23/07 |
| 28. (2) | PIPE Trades Dist. Council No. 36 | Mechanical Contractors Council of Central CA | 4/14/07 |
| 29. (2) | No. CA Carpenters Reg'l Council | Basic Crafts Worker' Compensation Benefits Trust | 8/30/07 |
| 30. (2) | No. CA District Council of Laborers | Basic Crafts Worker' Compensation Benefits Trust | 8/30/07 |
| 31. (2) | Operating Engineers Local 3 | Basic Crafts Worker' Compensation Benefits Trust | 8/30/07 |
| 32. (1) | Industrial, Professional & Technical Workers | Irish Construction | 12/20/07 |

Source: DWC